

UMBRELLA CLAUSES IN BILATERAL INVESTMENT
TREATIES: OF BREACHES OF CONTRACT, TREATY
VIOLATIONS, AND THE DIVIDE BETWEEN
DEVELOPING AND DEVELOPED COUNTRIES IN
FOREIGN INVESTMENT DISPUTES

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INTRODUCTION

Over the last decade, the face of international investment law has changed radically as an ever-increasing percentage of disputes over foreign investment are being resolved through international arbitration as opposed to diplomatic intervention or domestic lawsuits. The driving force behind this change has been the proliferation of the bilateral investment treaty (“BIT”), an agreement between two countries that governs the treatment of investments made in their respective territories by individuals and corporations from the other country.¹ The BIT serves to attract foreign investment by granting broad investment rights to investors and creating flexibility in the resolution of investment disputes. This flexibility typically includes allowing for any investment dispute to be resolved by international arbitration,² most often under the auspices of the International Centre for the Settlement of Investment Disputes (“ICSID”).³ In the last twelve years alone,

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¹ The already-substantial literature on BITs continues to expand apace with the growth of BITs. See, e.g., RUDOLF DOLZER & MARGARET STEVENS, *BILATERAL INVESTMENT TREATIES* (1995); U.N. Conference on Trade and Development (“UNCTAD”), *Bilateral Investment Treaties, 1959-1999*, Geneva, Switz., Dec. 2000, U.N. Doc. UNCTAD/ITE/IIA/2; UNCTAD, *Bilateral Investment Treaties In The Mid-1990s*, Geneva, Switz., Nov. 1998, U.N. Doc. UNCTAD/ITE/IIT/7 [hereinafter *Bilateral Investment Treaties in the Mid-1990s*]; KENNETH J. VANDEVELDE, *UNITED STATES INVESTMENT TREATIES: POLICY AND PRACTICE* (1992).

² See UNCTAD, *Dispute Settlement: Investor-State 41*, Geneva, Switz., May 2003, U.N. Doc. UNCTAD/ITE/IIT/30 (noting that in a survey of 335 BITs in force in 1992, 334 contained provisions for arbitration), available at <http://www.unctad.org/Templates/Download.asp?docid=3496&lang=1&intItemID=2314>.

³ See Christoph Schreuer, *Travelling the BIT Route -- Of Waiting Periods, Umbrella Clauses and Forks in the Road*, 5 J. WORLD INVESTMENT & TRADE 231, 231 (2004) (“Most [provisions in BITs for investor-State arbitration] refer to . . . ICSID.”); M. SORNARAJAH, *THE INTERNATIONAL LAW ON*

various countries concluded approximately 1,500 new BITs.⁴ This brings the total number of BITs to approximately 2,400, making the BIT one of the most widely used international agreements for protecting and influencing foreign investment.⁵ Not surprisingly, this dramatic increase in the use of BITs has led to a surge in the number of arbitrations involving investment treaties.⁶

One of the more controversial issues that has arisen in arbitration is the proper construction of the so-called “umbrella clause,” a provision found in many BITs that imposes a requirement on each Contracting State to observe all investment obligations entered into with investors from the other Contracting State. In particular, two recent ICSID decisions, *SGS v. Pakistan*⁷ and *SGS v. Philippines*,⁸ have brought to the forefront the question of whether the umbrella clause applies to obligations arising under otherwise independent investment contracts between the investor and the

FOREIGN INVESTMENT 251 (2d ed. 2004) (“Most dispute settlement provisions in investment treaties refer to ICSID arbitration.”) See also REED ET AL., GUIDE TO ICSID ARBITRATION 4 (2004) (noting that “many, if not most, BITs include the option of ICSID dispute resolution”). On the ICSID Convention, see Convention on the Settlement of Investment Disputes Between States and Nationals of Other States, Aug. 27, 1965, 17 U.S.T. 1270, 575 U.N.T.S. 159.

⁴ Susan D. Franck, *The Legitimacy Crisis in Investment Treaty Arbitration: Privatizing Public International Law Through Inconsistent Decisions*, 73 FORDHAM L. REV. 1521, 1522 (2005).

⁵ See UNCTAD, WORLD INVESTMENT REPORT 2005: TRANSNATIONAL CORPORATIONS AND INTERNATIONALIZATION OF R&D at 24, U.N. Doc. UNCTAD/WIR/2005, U.N. Sales No. E.05.IID.10 (2005) [hereinafter WORLD INVESTMENT REPORT] (stating that the total number of BITs worldwide was 2,392 as of the end of 2004), available at http://www.unctad.org/en/docs/wir2005_en.pdf; Jeswald W. Salacuse & Nicholas P. Sullivan, *Do BITs Really Work?: An Evaluation of Bilateral Investment Treaties and Their Grand Bargain*, 46 HARV. INT’L L. J. 67, 67 (2005); see also SHERIF H. SEID, GLOBAL REGULATION OF FOREIGN DIRECT INVESTMENT 51 (2002) (noting that “in just over four decades, the bilateral investment treaty has become of the most important legal instruments affecting foreign investment”).

⁶ Whereas only a handful of arbitrations involved claims under investment treaties before the mid 1990s, over ninety such arbitrations have been registered with ICSID alone, encompassing claims ranging anywhere from 100 million to billions of dollars. Franck, *supra* note 4, at 1521; see Stanimir A. Alexandrov, *Breaches of Contract and Breaches of Treaty --The Jurisdiction of Treaty-based Arbitration Tribunals to Decide Breach of Contract Claims in SGS v. Pakistan and SGS v. Philippines*, 5 J. WORLD INVESTMENT & TRADE 555, 555 (2004); see also Schreuer, *supra* note 3, at 231 (noting that “[i]n recent years, the majority of cases in investment arbitration have been based on bilateral investment treaties”).

⁷ *Société Générale de Surveillance S. A. v. Pakistan*, Decision of the Tribunal on Objections to Jurisdiction, ICSID (W. Bank) Case No. ARB/01/13 (2003), available at <http://www.worldbank.org/icsid/cases/SGS-decision.pdf>. The Members of the Tribunal were Judge Florentino P. Feliciano (President), André Faurès and J. Christopher Thomas. *Id.*

⁸ *Société Générale de Surveillance S. A. v. Philippines*, Decision of the Tribunal on Objections to Jurisdiction, ICSID (W. Bank) Case No. ARB/02/6 (2004), reprinted in 19 MEALEY’S INT’L. ARB. REP. 6 (2004). The Members of the Tribunal were Ahmed S. El-Koshery (President), James Crawford and Antonio Crivellaro. *Id.*

host State. The significance of such an application is that the international arbitration tribunal constituted under the BIT (the “BIT tribunal”) would thereby have jurisdiction over breach-of-contract claims since a breach of the investment contract is also a breach of the umbrella clause. Critically, this means that the investor can now seek redress of a breach of any investment contract between it and a Contracting State through international arbitration under the BIT.

While purporting to shed light on this question, the *SGS* decisions have only confused the issue by adopting conflicting yet self-defeating interpretations of the umbrella clause that result in its nullification. To wit: *SGS v. Pakistan* determined that a BIT tribunal does not have jurisdiction over contractual claims on the ground that umbrella clauses do not in general extend to such claims,⁹ whereas *SGS v. Philippines*, though deciding to the contrary that a BIT tribunal in fact has such jurisdiction, went on to determine that it should not exercise this jurisdiction where the contract contains an exclusive forum selection clause designating a different forum for resolving disputes arising under the contract.¹⁰

In focusing on the *SGS* decisions, this article seeks to answer the two principal issues raised therein, namely:

- (1) Whether a BIT tribunal may exercise jurisdiction over breach-of-contract claims on the ground that the umbrella clause applies to investor-State contracts; and if so,
- (2) Whether a BIT tribunal may exercise such jurisdiction when the contract contains an exclusive forum selection clause designating a different forum for the resolution of contractual disputes.

Contrary to the *SGS* decisions, this article answers both questions in the affirmative. It concludes that the better interpretation is that an umbrella clause enables a BIT tribunal to exercise jurisdiction over claims concerning such breaches of contract, which are also BIT violations under the clause, and further permits the tribunal to do so notwithstanding an exclusive forum selection clause in the contract. Indeed, as detailed below, any other interpretation of the umbrella clause, including those advanced by the *SGS* decisions, effectively eviscerates the umbrella clause, and is at odds with the clear language and purpose of the clause as reflected in its history.¹¹ In particular, the *SGS* interpretations would deprive the investor of the ability to resolve contractual investment disputes in a neutral and international forum, an intended core benefit of BITs. When the agreement be-

⁹ See *Pakistan*, ICSID (W. Bank) Case No. ARB/01/13 ¶¶ 163-174.

¹⁰ See *Philippines*, ICSID (W. Bank) Case No. ARB/02/6 ¶¶ 113-129, 136-155

¹¹ See *infra* Part IV.

tween the Contracting States affirmatively provides for such a benefit, the host State must be held to its side of the bargain.¹²

More broadly, however, this article not only analyzes how the umbrella clause should operate, it also considers its place in the historical context of the development of foreign investment law in recent decades. From this vantage, the application of the umbrella clause reveals not just the differences between breaches of contract and treaty violations, but something altogether less obvious. One sees that the debate over interpretation is actually the latest incarnation of a long-standing and continuing conflict between the investment interests of developing countries and developed countries.

Historically, foreign investment capital flows from developed to developing countries. As a result, a significant proportion of BITs are between developed countries on the one hand and developing countries on the other. For the same reason, in many such arrangements, the investor is from a developed country and the host State is a developing country. Therefore, even though such a BIT imposes reciprocal obligations on both Contracting States, its *effects* are asymmetrical. The result is that developing countries seek to interpret restrictively any BIT provision that accords rights to the investor and imposes obligations on the host State, whereas developed countries will read the same provision expansively. The umbrella clause is just such a BIT provision. Thus, the disagreement over umbrella clauses in this scenario is in effect an extension of the enduring tension between developing and developed countries on foreign investment.

More than just a historical exercise, this broader perspective of the umbrella clause anticipates a potentially divisive objection to the interpretation of umbrella clauses proposed here. Namely, by favoring the investor, the interpretation sides with the developed country against the developing country, which presumably has less bargaining power in negotiating a BIT. In other words, to enforce the umbrella clause is potentially to enforce an unconscionable contract involving a developing country under economic pressure to enter into a BIT with an umbrella clause. But this argument is misplaced. For one thing, it may equally be contended that the presence of an exclusive forum selection clause in an investment contract designating domestic courts reflects a similar disparity in bargaining power between the host State and the investor, and to enforce such a clause is to enforce an unconscionable contract that unfairly penalizes the *investor*.¹³ Indeed, as between the two, the enforcement of the umbrella clause, rather than the forum selection clause, inspires more confidence that a just result will follow since the former allows disputes to be resolved through international

¹² See *infra* Part IV.C.

¹³ See *infra* Part V.B.

arbitration—a neutral forum in which both parties have an equal say in the appointment of the tribunal—whereas the latter requires disputes to be resolved by a domestic court whose own government is an interested party in the process.

Further, carried to the extreme, such an argument would invalidate not just the umbrella clause, but all BIT provisions. Fatally, the argument also assumes that the bargain is one-sided, when, in fact, the host State stands to benefit from the adoption of BIT provisions such as the umbrella clause because they foster a more hospitable, and therefore, more attractive, environment for foreign investment. Allowing the host State to renege on its agreement in the BIT creates uncertainty in the global marketplace and can serve only to discourage foreign investment. In particular, when dealing with a provision such as the umbrella clause, whose language, history, and purpose dictate but one reasonable interpretation—that it applies without exception to investment contracts—it is difficult to see why it should not be enforced in accordance with the parties' agreement. Rather, the more broadly applicable principle is that of the sanctity of contract, not simply as between the host State and the investor over an investment contract, but also as between the Contracting States over a BIT.

To lay the foundation for this more fundamental perspective of umbrella clauses, Part I of the article begins by briefly describing the history and evolution of foreign investment law and the BIT. Part II looks at the origins and purpose of umbrella clauses. Part III sets out the decisions involving umbrella clauses, including the *SGS* cases. Part IV critically examines these decisions and advances a different interpretation of the umbrella clause more consistent with its language and purpose. Finally, Part V pans back to take a historical view of the debate over the umbrella clause in the wider context of foreign investment disputes between developed and developing countries.

I. A BRIEF HISTORY OF FOREIGN INVESTMENT LAW AND THE BIT

As the global economy began to normalize following World War II, foreign capital flowed more freely and the significance of foreign investment grew.¹⁴ While things were looking up for foreign investment, the same could not necessarily be said for foreign investors. In particular, there was no coherent legal framework in place to their interests. Foreign investors looking to rely on international investment law found only “an ephemeral structure consisting largely of scattered treaty provisions, a few question-

¹⁴ See Salacuse & Sullivan, *supra* note 5, at 68.

able customs, and contested general principles of law.”¹⁵ This untidy collection of laws was woefully inadequate. For example, it failed to account for contemporary investment practices, or even to offer investors an effective enforcement mechanism to pursue their claims against host countries that seized their interests or repudiated their contractual obligations.¹⁶ There was simply no clear articulation of the rights and obligations of investors and host states respectively. The few and frequently vague international legal principles that existed concerning such rights and obligations were subject to varying interpretation, engendering sharp disagreement between industrialized countries and the newly decolonized developing states. While developed countries asserted that international law imposed an obligation on host states to protect foreign investments and to provide compensation for injuring or seizing those interests, developing countries rejected such a view on the grounds that it perpetuated the economic dominance of developed over developing countries, and infringed on their sovereignty by circumscribing their ability to control economic activities within their borders.¹⁷

However, with the continuing rapid expansion of foreign investment, both sides had growing incentive to create a more conducive legal environment for international investments. Early attempts to build such a regime took the form of proposals for multilateral investment treaties, including the 1948 Havana Charter and the 1949 International Chamber of Commerce International Code of Fair Treatment of Foreign Investment.¹⁸ However, along with many subsequent efforts to establish multilateral treaties,¹⁹ these early proposals failed in part because they had to address wide-ranging interests of multiple countries that were ultimately too striated to reconcile.²⁰

Faced with failure at the multilateral level, individual European countries began a pioneering effort to negotiate foreign investment treaties with

¹⁵ *Id.*

¹⁶ *See id.* at 68.

¹⁷ *See id.* at 69.

¹⁸ Franziska Tschofen, *Multilateral Approaches to the Treatment of Foreign Investment*, 7 ICSID REV.-FOREIGN INVESTMENT L.J. 384 (1992) (surveying various attempts to create multilateral treaties on foreign investment).

¹⁹ Such multilateral efforts included the proposed 1957 International Convention for the Mutual Protection of Private Property Rights in Foreign Countries, the 1959 Abs-Shawcross Draft Convention, and the 1967 Organization for Economic Cooperation and Development (“OECD”) Draft Convention on the Protection of Foreign Property. Salacuse & Sullivan, *supra* note 5, at 72.

²⁰ Franck, *supra* note 4, at 1526 (noting that initiatives for multilateral treaties were largely unsuccessful because of “difficulties in promulgating sweeping reforms on a multilateral basis”). *See generally* Tschofen, *supra* note 18 (discussing various attempts to create multilateral treaties on foreign investment).

developing countries on a one-to-one basis.²¹ Their success ushered in the first modern bilateral investment treaties or BITs, and subsequently spurred industrialized nations outside Europe to enter into their own BITs with individual developing countries. By 1970, just eleven years after Germany and Pakistan concluded the first BIT, developing and developed countries had concluded a total of eighty-three BITs.²² In the period following the late 1980s, the BIT movement again made a quantum leap forward as emerging economies in Eastern and Central Europe, Asia, Africa and South America opened their markets in pursuit of foreign capital.²³ Whereas nations had signed a little over 300 BITs by the end of 1988,²⁴ there were close to 2,400 BITs in place at the end of 2004.²⁵

As its name suggests, a BIT is an agreement between two countries that governs the treatment of investments made in the territory of each state by individuals or companies from the other state. Although many countries rely on their own model agreements when negotiating individual BITs, BITs are remarkably similar in their organization and content. In general, BITs address four substantive issues: (1) conditions for the admission of foreign investors to the host State; (2) standards of treatment of foreign investors; (3) protection against expropriation; and (4) methods for resolving investment disputes.²⁶

BITs are also very similar in that they typically contain definitions of investments,²⁷ which are often broad,²⁸ including the investment's time element. Accordingly, many BITs cover both existing and future investments.²⁹ Thus, BITs not only provide incentive for future investment, but can also have the effect of encouraging foreign investors to maintain existing investments.

²¹ See Salacuse & Sullivan, *supra* note 5, at 73.

²² UNCTAD, *BILATERAL INVESTMENT TREATIES: 1959-1991* at 3, U.N. Sales No. E.92.II.A.16 (1992) (noting that there were "83 treaties in the 1960s").

²³ See *id.* at 4.

²⁴ See Athena J. Pappas, *References on Bilateral Investment Treaties*, 4 ICSID REV.-FOREIGN INVESTMENT L.J. 189, 194-203 (1989).

²⁵ WORLD INVESTMENT REPORT, *supra* note 5, at 24.

²⁶ George M. von Mehren et al., *Navigating Through Investor-State Arbitrations: An Overview of Bilateral Investment Treaty Claims*, DISP. RESOL. J., Feb.-Apr. 2004, at 69, 70. See also SEID, *supra* note 5, at 52.

²⁷ See SEID, *supra* note 5, at 52.

²⁸ See *Fedax N.V. v. Venezuela*, Decision of the Tribunal on Objections to Jurisdiction, ICSID (W. Bank) Case No. ARB/96/3 (1997), reprinted in 37 I.L.M. 1378, 1385 (1998) (noting that a "broad definition of investment . . . is not at all an exceptional situation. On the contrary, most contemporary bilateral treaties of this kind refer to 'every kind of asset' or to 'all assets.'").

²⁹ SEID, *supra* note 5, at 52. There are, however, a few BITs that limit their coverage to investments at the time the treaty was concluded. *Id.*

Significantly, only states (and not the investors) enter into BITs. Notwithstanding, the investor is able to enforce directly its rights under the BIT through the BIT's dispute settlement provisions. These provisions typically authorize the investor to submit an investment dispute between it and a Contracting State to the investor's choice of forums, often including international arbitration through ICSID. Thus, when a state enters into a BIT, it effectively extends a standing offer to eligible investors to arbitrate any relevant investment dispute through international arbitration. Should the investor choose to accept the offer, it may do so often by simply initiating arbitration proceedings, thereby perfecting the parties' agreement to arbitrate the investment dispute.³⁰

From the investor's perspective, this ability to submit an investment dispute to international arbitration is one of the BIT's chief benefits. As that feature is at the heart of the umbrella clause, its interpretation has significant implications for the investor.

II. THE ORIGINS OF THE UMBRELLA CLAUSE³¹

Known variously as the mirror or parallel effect clause or *pacta sunt servanda* (i.e., sanctity of contract clause),³² the umbrella clause is a treaty provision found in many BITs that requires each Contracting State to observe all investment obligations it has assumed with respect to investors from the other Contracting State.³³ The idea behind the metaphor is that an

³⁰ This process is described in more detail in Jan Paulsson, *Arbitration Without Privity*, 10 ICSID REV.-FOREIGN INVESTMENT L.J. 232 (1995). See also REED ET AL., *supra* note 3, at 35, which notes that:

In non-contractual arbitration, the parties express their consent in two steps, each in turn. First, the host State consents by including a standing offer to submit to ICSID jurisdiction in its national legislation or in a bilateral or multilateral investment treaty. Second, the investor . . . consents by accepting that offer later, either in writing to the host State at any time or by filing a request to arbitrate with ICISD. In this way, the parties' agreement to arbitrate is perfected.

³¹ For a fuller treatment of the history of the umbrella clause, see Anthony C. Sinclair, *The Origins of the Umbrella Clause in the International Law of Investment Protection*, 20 ARB. INT'L 411, 413-18 (2004). In summarizing the history of the umbrella clause, this Part relies primarily on Sinclair's article.

³² See, e.g., *Société Général de Surveillance S. A. v. Pakistan*, Decision of the Tribunal on Objections to Jurisdiction, ICSID (W. Bank) Case No. ARB/01/13, ¶ 163 (2003), available at <http://www.worldbank.org/icsid/cases/SGS-decision.pdf>.

³³ Judith Gill et al., *Contractual Claims and Bilateral Investment Treaties: A Comparative Review of the SGS Cases*, 21 J. INT'L ARB. 397, 403 n.31 (2004) (finding that approximately 40% of a sample of BITs taken from INVESTMENT TREATIES (ICSID ed., 2003) contained umbrella clauses). An example of an umbrella clause is Article X of the Switzerland-Philippines BIT, which provides that "[e]ach Contracting Party shall observe any obligation it has assumed with regard to specific investments in its territory by investors of the other Contracting Party." See *Société Général de Surveillance S. A. v.*

umbrella clause brings otherwise independent investment arrangements between a Contracting State and private investors from the other Contracting State under the treaty's "umbrella of protection."³⁴ Its purpose is to create an inter-state obligation to observe investment agreements that investors may enforce when the BIT confers a direct right of recourse to arbitration. More specifically, the history of the umbrella clause makes clear that it was designed to allow for any breach of a relevant investment contract to be resolved under the treaty in an international forum.

Under general international law, it is unclear whether a state breaching a contract with an investor qualifies *per se* as a violation of an international obligation.³⁵ Such a breach may simply be treated as a domestic commercial matter. As such, investors were often forced to resolve any disputes over their contracts with the host state in that state's municipal courts and under its domestic laws, which were vulnerable to unilateral variation by the state.³⁶ It was in this context that the umbrella clause first arose. Specifically, scholars have traced its origins to a 1954 draft settlement agreement involving the Anglo-Iranian Oil Company's ("AIOC") claims regarding Iran's oil nationalization program.³⁷

In 1951, AIOC's interests under a long-standing oil concessionary contract with Iran were effectively expropriated when a change in government led to the enactment of the Iranian Oil Nationalization Law, which placed all oil operations in Iran in the government's hands.³⁸ Thereafter, AIOC pursued a range of ultimately unsuccessful legal options for redress, including a failed attempt to arbitrate the claims pursuant to what turned out

Philippines, Decision of the Tribunal on Objections to Jurisdiction, ICSID (W. Bank) Case No. ARB/02/6, ¶ 34 (2004), *reprinted in* 19 MEALEY'S INT'L. ARB. REP. 6 (2004).

³⁴ See Sinclair, *supra* note 31, at 412-13.

³⁵ LASSO OPPENHEIM, ROBERT JENNINGS & ARTHUR WATTS, OPPENHEIMER'S INTERNATIONAL LAW 927 (9th ed. 1992) ("It is doubtful whether a breach by a state of its contractual obligations with aliens constitutes *per se* a breach of an international obligation . . ."); Gill et al., *supra* note 33, at 403 (noting that "a violation of a contract entered into a state with an investor of another state is not, by itself, a violation of international law"); Schreuer, *supra* note 3, at 249-50 ("It is generally accepted that not every breach of contract by a State automatically amounts to a violation of international law . . .").

³⁶ See, e.g., Sinclair, *supra* note 31, at 415-16 (describing how a long-standing oil concessionary contract of the Anglo-Iranian Oil Company with Iran was effectively expropriated when a change in certain leadership positions in government led to the enactment of the Iranian Oil Nationalization Law, which required all oil operations in Iran to be carried out by the Iranian government); see also International Bank for Reconstruction and Development, Report of the Executive Directors on the Convention on the Settlement of Investment Disputes between States and Nationals of Other States (Mar. 18, 1965), <http://www.worldbank.org/icsid/basicdoc/partB-section03.htm> (noting in 1965 that "investment disputes are as a rule settled through administrative, judicial or arbitral procedures available under the laws of the country in which the investment concerned is made").

³⁷ Sinclair, *supra* note 31, at 415-16.

³⁸ *Id.* at 414.

to be a defective provision in the concession agreement³⁹ and abortive proceedings before the ICJ.⁴⁰ It was not until a U.S.-sponsored coup in Iran returned to power officials friendly to foreign interests that the dispute was settled.⁴¹

In accordance with advice provided by Elihu Lauterpacht to AIOC, the proposed settlement was to be comprised of two instruments: (a) a “Consortium Agreement” between Iran and a consortium of oil companies including AIOC that would continue to operate certain Iranian oil facilities; and (b) an “umbrella treaty” between Iran and the United Kingdom incorporating the Consortium Agreement and containing a guarantee by Iran to fulfill the terms thereof.⁴² To counter the conspicuous failure of the earlier concession agreement to protect AIOC’s interests, the proposed settlement was deliberately structured such that any contract between Iran and AIOC would be “incorporated or referred to in a treaty between Iran and the United Kingdom in such a way that a breach of the contract or settlement shall be *ipso facto* deemed to be a breach of the treaty.”⁴³

The umbrella treaty both ensured that the settlement would not be exclusively governed by Iranian law (and otherwise vulnerable to its unilateral variance), and provided an interstate remedy allowing for any breach of the settlement to be resolved by the ICJ instead of the Iranian courts.⁴⁴ As it turned out, the settlement took a different direction and the umbrella treaty never materialized.⁴⁵

Just a few years later, however, the umbrella clause resurfaced in a more concrete form in the 1959 Abs-Shawcross Draft Convention of Investments Abroad (“Abs-Shawcross Draft”).⁴⁶ A private effort to draft rules

³⁹ See Elihu Lauterpacht, *International Law and Private Foreign Investment*, 4 IND. J. GLOBAL LEGAL STUD. 259, 271-72 (1997).

⁴⁰ AIOC prevailed on the British Government, a major shareholder of AIOC, to initiate claims against Iran with the International Court of Justice, which declined to exercise jurisdiction over the dispute. Specifically, the Court found that it lacked jurisdiction over the dispute because the terms of Iran’s acceptance of the Court’s compulsory jurisdiction did not extend to allegations of breach of customary international law, as opposed to treaties. Sinclair, *supra* note 31, at 415; Anglo-Iranian Oil Co. Ltd. (U.K. v. Iran), 1952 I.C.J. 93 (July 22), available at http://www.icj-cij.org/icjwww/idecisions/i_summaries/iukisummary520722.htm.

⁴¹ See Sinclair, *supra* note 31, at 415.

⁴² *Id.* at 415-16.

⁴³ *Id.* at 415.

⁴⁴ *Id.* at 416-17.

⁴⁵ *Id.* at 417.

⁴⁶ The text of the Abs-Shawcross Draft is reprinted in *The Proposed Convention to Protect Private Foreign Investment: A Round Table*, 9 J. PUB. L. 115, 116-18 (1960) [hereinafter Abs-Shawcross Draft].

for the protection of foreign investments,⁴⁷ European lawyers created the Abs-Shawcross Draft in part to address the kinds of investment disputes that confronted AIOC.⁴⁸ Article II, the umbrella clause, provides as follows: “Each party shall at all times ensure the observance of any undertakings which it may have given in relation to investments made by nationals of any other Party.”⁴⁹

Notably, this umbrella clause, unlike its predecessor in the proposed AIOC settlement, applies not just to one particular agreement but to all investment commitments undertaken by each state party with investors from any other state party. In this way, the umbrella clause evolved to resemble more closely the umbrella clause in modern BITs.

Additionally, in requiring “the observance of *any undertakings*,” the Abs-Shawcross Draft plainly included all contractual investment obligations within its scope, including those between a state and foreign private investors,⁵⁰ since an “undertaking” is generally understood to be broader than a contract and thus encompasses obligations arising from a contract.⁵¹ Commentators at the time drew the same conclusion, including Fatouros, who observed that Article II was “meant to cover the cases of contractual commitments of states to aliens,”⁵² and Schwarzenberger, who noted that it “covers undertakings by contracting parties both to subjects and objects of international law.”⁵³

⁴⁷ More specifically, the Abs-Shawcross Draft was the product of a private effort by two groups of European lawyers led respectively by Hermann Abs, the then Chairman of Deutsche bank, and by Hartley Shawcross, the former British Attorney-General, hence the name of the draft convention. See Abs-Shawcross Draft, *supra* note 46, at 115.

⁴⁸ See Sinclair, *supra* note 31, at 418-420 (noting that a separate draft convention that was effectively a precursor to the Abs-Shawcross Draft “was an openly acknowledged attempt to remedy the failures reflected in such cases as *Anglo-Iranian Oil Company*”).

⁴⁹ Abs-Shawcross Draft, *supra* note 46, at 116.

⁵⁰ See Sinclair, *supra* note 31, at 421 (“The text of Article II refers to ‘*any undertakings*.’ There can be no doubt that it was the author’s intention to protect, *inter alia*, contractual undertakings entered into between states and foreign private investors.”).

⁵¹ “[U]ndertakings” appears to be a concept wider than that of “contract” in the technical sense of the word. An “undertaking” can, for example, describe the situation arising out of a general promise made by a State to accord to foreign investors a particular standard of treatment, followed by an actual investment made in reliance on that promise.

Sinclair, *supra* note 31, at 428 (quoting Elihu Lauterpacht, *Drafting of Conventions for the Protection of Investment*, in INT’L COMP. L.Q., THE ENCOURAGEMENT AND PROTECTION OF INVESTMENT IN DEVELOPING COUNTRIES 218, 229 (3d ed. Supp. 1962)).

⁵² Arghyrios A. Fatouros, *An International Code to Protect Private Investment—Proposals and Perspectives*, 14 U. TORONTO L.J. 77, 88 n.80 (1961).

⁵³ Georg Schwarzenberger, *The Abs-Shawcross Draft Convention on Investments Abroad: A Critical Commentary*, 9 J. PUB. L. 147, 154 (1960).

That the umbrella clause should be interpreted to include such contracts is consistent with its purpose. The authors of the draft Convention explained that Article II “affirms, and attributes specific content to, the universally accepted principle *Pacta sunt servanda*,”⁵⁴ and explicitly noted that the principle “applies not only to agreements directly concluded between States, but also to those between a State and foreigners”⁵⁵ Thus, the drafters intended that Article II insure a remedy lay under international law for any breach of a state-investor contract subject to the draft convention, i.e., that the “purpose of that clause [was] to dispel whatever doubts may possibly exist as to whether a unilateral violation of a concession contract is an international wrong.”⁵⁶

Significantly, the Abs-Shawcross Draft went on to influence certain draft conventions of the Organization for Economic Cooperation and Development (“OECD”), including the 1967 OECD Draft Convention on the Protection of Foreign Property (“OECD Draft”).⁵⁷ Article 2 of the OECD Draft is an umbrella clause that provides as follows: “Each Party shall at all times ensure the observance of undertakings given by it in relation to property of nationals of any other Party.”⁵⁸

According to the official commentary to the OECD Draft, Article 2 is “an application of the general principle of *pacta sunt servanda*” to “agreements between States and foreign nationals.”⁵⁹ Additionally, the commentary not only makes clear that “[a]n undertaking may be embodied in a *contract or in a concession*,”⁶⁰ but that “any right originating under such an undertaking gives rise to an *international right*.”⁶¹ In sum, Article 2 was clearly meant to extend to investor-State contracts and its purpose was to allow obligations arising there under (i.e., contractual obligations) to be

⁵⁴ Abs-Shawcross Draft, *supra* note 46, at 120.

⁵⁵ *Id.* (internal quotations and citation omitted).

⁵⁶ Ignaz Seidl-Hohenveldern, *The Abs-Shawcross Draft Convention to Protect Private Foreign Investment: Comments on the Round Table*, 10 J. PUB. L. 100, 104-05 (1961); *see also* Schwarzenberger, *supra* note 53, at 154-55:

If a breach of [an undertaking is given in relation to investments] is alleged . . . any such act or omission may amount to a breach of the Convention and, thus, constitute an arbitrable dispute under the Convention. . . . The effect of [Article II] is to transform obligations towards objects of international law, which as such are beyond the pale of international law, into obligations under international law.

⁵⁷ *See* OECD, *Draft Convention on the Protection of Foreign Property and Resolution of the Council of the OECD on the Draft Convention*, OECD Publication No. 23081 (October 12, 1967), reprinted in 7 INT’L LEGAL MATERIALS 117 (1968).

⁵⁸ *Id.* at 123.

⁵⁹ *Id.*

⁶⁰ *Id.* (emphasis added).

⁶¹ *Id.* (emphasis in original).

characterized as treaty obligations, thereby securing their protection under international law.

As Lauterpacht noted, Article 2's effect was to "put [investor-State contracts] on a special plane in that breach of them becomes immediately a breach of convention."⁶² Likewise, Prosper Weil, another distinguished commentator at that time, pointed out that:

There is, in fact, no particular difficulty when there is an "umbrella treaty" between the contracting State and the State of the other party, which turns the obligation to perform the contract into an international obligation of the contracting State *vis-à-vis* the State of the other contracting party. The intervention of the umbrella treaty transforms the contractual obligations thereby ensuring, as it has already been stated, "the inviolability of the contract under threat of violating the treaty"; any non-performance of the contract, even if it is legal under the national law of the contracting State, gives rise to the international liability of the latter *vis-à-vis* the State of the other contracting party.⁶³

In conjunction with dispute resolution provisions in the convention, the umbrella clause would allow for breaches of investor-State contracts to be resolved as a matter of international law in an international forum.⁶⁴ Relevantly, the International and Comparative Law Section of the American Bar Association noted that the OECD Draft "would provide for giving effect in an international forum to acquired rights arising from State contracts, and in this way would ensure the application of an international standard where under international law that standard should be applied."⁶⁵

Although the OECD Draft ultimately failed to pass, the OECD Council resolved at its 150th Meeting in 1967 to recommend the draft convention to member states as a model for their own BITs and as a general affirmation of international law rules applicable to foreign investment.⁶⁶

Indeed, umbrella clauses had in the meantime already found their way into BITs, including the first known BIT, the Germany-Pakistan BIT of 1959.⁶⁷ Article 7 of that BIT provides as follows: "Either party shall ob-

⁶² Lauterpacht, *supra* note 51.

⁶³ Alexandrov, *supra* note 6, at 566-7 (quoting in his own translation Prosper Weil, *Problèmes relatifs aux contrats passés entre un Etat et un particulier*, in 128 *Recueil des Cours* 95, 130 (1969)). See also Schreuer, *supra* note 3, at 250-51 (quoting the same in his own but substantially similar translation).

⁶⁴ See Sinclair, *supra* note 31, at 430 (noting in relation to the umbrella clause in the OECD Draft that "when coupled with a watertight dispute settlement provision the umbrella clause would create an enforceable international obligation to observe investment contracts").

⁶⁵ COMM. ON INT'L TRADE & INV., SECTION ON INT'L & COMPARATIVE LAW, AM. BAR ASS'N, THE PROTECTION OF PRIVATE PROPERTY INVESTED ABROAD 96 (1963).

⁶⁶ OECD, *supra* note 57.

⁶⁷ See Treaty for the Promotion and Protection of Investments, F.R.G.-Pak., Nov. 25, 1959, 457 U.N.T.S. 23, 28-29 (1963).

serve any other obligation it may have entered into with regard to investments by nationals or companies of the other Party.”⁶⁸ A German commentator observed in his survey of German BITs that such an umbrella clause “relates particularly to investment contracts between the investor and the host country” and “transforms responsibility incurred towards a private investor under a contract into international responsibility.”⁶⁹ He also noted that “[t]he protection of such contracts is now a standard clause in bilateral investment agreements.”⁷⁰

The 1959 Germany-Pakistan BIT would lay the foundation for the 1991 German Model BIT, Article 8(2) of which is an umbrella clause with substantially similar language: “Each Contracting Party shall observe any other obligation it has assumed with regard to investments in its territory by nationals or companies of the other Contracting Party.”⁷¹

The U.S. Model BIT of 1983, which was designed with the OECD Draft in mind,⁷² also contains an umbrella clause providing that “[e]ach Party shall observe any obligation it may have entered into with regard to investors or nationals or companies of the other Party.”⁷³ Subsequent U.S. Model BITs published in 1984 and 1987 include similarly worded umbrella clauses.⁷⁴ Again, commentators analyzing these umbrella clauses agree on their effects, namely that such a clause “raises to a treaty issue any attempt by a BIT partner to invalidate a contract by changes in domestic law or otherwise . . . [such that] a breach of contract constitutes a breach of treaty.”⁷⁵

⁶⁸ *Id.* at 28.

⁶⁹ Joachim Karl, *The Promotion and Protection of German Foreign Investment Abroad*, 11 ICSID REV.-FOREIGN INVESTMENT L.J. 1, 23 (1996).

⁷⁰ *Id.*

⁷¹ 1991 German Model Treaty on the Encouragement and Reciprocal protection of Investments, Sept. 1991, *reprinted in* 11 ICSID REV.-FOREIGN INVESTMENT L.J. 221, 226 (1996).

⁷² See K. Scott Gudgeon, *United States Bilateral Investment Treaties: Comments on their Origin, Purposes and General Treatment Standards*, 4 INT’L TAX AND BUS. L. 105, 111 (1986) (noting that the US Model BIT was “specifically designed to dovetail with efforts of the OECD”).

⁷³ 1983 U.S. Model BIT art. II(4), Jan. 21, 1983, *reprinted in* VANDELDE, *supra* note 1, at App. A-2.

⁷⁴ See 1984 U.S. Model BIT art. II(2), Feb. 24, 1984, *reprinted in* VANDELDE, *supra* note 1, at App. A-3 (“Each Party shall observe any obligation it may have entered into with regard to investments.”); 1987 U.S. Model BIT art. II(2), Sept. 1987, *reprinted in* VANDELDE, *supra* note 1, at App. A-4 (same).

⁷⁵ Gudgeon, *supra* note 72, at 126. See also VANDELDE, *supra* note 1, at 78 (“Under this clause [in the US Model BIT], a party’s breach of an investment agreement with an investor becomes a breach of the BIT.”).

Due in part to the influence of the OECD Draft, which has likewise influenced the BITs of other major developed economies, including France⁷⁶ and the United Kingdom,⁷⁷ the umbrella clause is now commonplace in BITs.⁷⁸ Consistent with the commentary noted above concerning particular umbrella clauses, wide-ranging surveys of BITs generally affirm that umbrella clauses allow breaches of investor-State contracts to be characterized as BIT violations so as to trigger dispute resolution procedures provided under the BIT. For example, the United Nations Centre on Transnational Corporations noted that an umbrella clause “makes the respect of [investor-State] contracts . . . an obligation under the treaty. Thus, a breach of such a contract by the host State would engage its responsibility under the [BIT] and—unless direct dispute settlement procedures come into play—entitle the home State to exercise diplomatic protection of the investor.”⁷⁹ Similarly, the United Nations Conference on Trade and Development (UNCTAD) observed in its survey of BITs in the mid-1990s that “as a result of [an umbrella clause in a BIT], violations of commitments regarding investment by the host country would be redressible through a BIT.”⁸⁰

Thus, the sum of its history and the virtually uniform body of opinion concerning its interpretation points unambiguously to one conclusion: The umbrella clause applies to obligations arising under investor-State contracts so as to allow for their breach to be resolved as BIT violations. In spite of this background, however, the first two decisions to consider closely the umbrella clause, *SGS v. Pakistan*⁸¹ and *SGS v. Philippines*,⁸² arrived at in-

⁷⁶ See Sinclair, *supra* note 31, at 433 (noting that the French model BIT was based on the 1967 OECD Draft) (citing P. Julliard, *Le Réseau Français des conventions bilatérales d'investissements: à la recherche d'un droit perdu?*, 13 DROIT ET PRATIQUE DU COMMERCE INTERNATIONALE 9, 16 (1987) (Fr.)).

⁷⁷ See Eileen Denza and Shelagh Brooks, *Investment Protection Treaties: United Kingdom Experience*, 36 INT'L & COMP. L.Q. 908, 910 (1987) (noting the influence of the OECD Draft on U.K. BITs).

⁷⁸ See Karl, *supra* note 69 (noting that “[t]he protection of such contracts is now a standard clause in bilateral investment agreements . . .”).

⁷⁹ UNITED NATIONS CENTRE ON TRANSNATIONAL CORPORATIONS, BILATERAL INVESTMENT TREATIES 39 (1988).

⁸⁰ *Bilateral Investment Treaties in the mid-1990s*, *supra* note 1, at 56. The study also notes that “the language of [a typical umbrella clause in a BIT] is so broad that it could be interpreted to cover all kinds of obligations, explicit or implied, contractual or non-contractual, undertaken with respect to investment generally.” *Id.*

⁸¹ See Société Générale de Surveillance S. A. v. Pakistan, Decision of the Tribunal on Objections to Jurisdiction, ICSID (W. Bank) Case No. ARB/01/13 (2003), available at <http://www.worldbank.org/icsid/cases/SGS-decision.pdf>.

⁸² See Société Générale de Surveillance S. A. v. Philippines, Decision of the Tribunal on Objections to Jurisdiction, ICSID (W. Bank) Case No. ARB/02/6 (2004), reprinted in 19 MEALEY'S INT'L ARB. REP. 6 (2004).

terpretations that while inconsistent with one another, have the common effect of overturning that conclusion.

III. DECISIONS INVOLVING THE UMBRELLA CLAUSE

A. *SGS v. Pakistan*

In *SGS v. Pakistan*, SGS, a Swiss company, contracted with the Republic of Pakistan in 1994 to provide “pre-shipment inspection” (“PSI”) services with respect to certain goods destined for Pakistan.⁸³ Under the agreement (the “PSI Agreement”), SGS undertook to inspect goods imported into Pakistan with the objective of increasing custom revenues collection by ensuring that the goods were properly classified for customs purposes.⁸⁴ Some years into the contract, however, Pakistan became dissatisfied with SGS’s performance, and terminated the contract.⁸⁵ Thereafter, Pakistan commenced arbitration proceedings in Pakistan in accordance with Article 11 of the PSI Agreement, which provided that any dispute arising out of the PSI Agreement “shall be settled by arbitration in accordance with the Arbitration Act of Pakistan”⁸⁶

In turn, however, SGS initiated proceedings in a different forum. It submitted instead a Request for Arbitration to ICSID,⁸⁷ alleging that Pakistan’s conduct under the PSI Agreement violated its obligations under the Switzerland-Pakistan BIT, which the two countries had concluded in the interim in 1995.⁸⁸ Specifically, SGS alleged that Pakistan’s actions constituted violations of various BIT provisions that established substantive standards for the treatment of investments, including, for example, Pakistan’s requirements under Articles 4(1) and 4(2) respectively to “protect” and ensure the “fair and equitable” treatment of Swiss investments in Pakistan.⁸⁹ Additionally, SGS claimed that Pakistan was liable under the BIT for all breaches of *the PSI agreement* by virtue of the umbrella clause in the BIT

⁸³ *Pakistan*, ICSID (W. Bank) Case No. ARB/01/13 ¶ 11.

⁸⁴ *Id.* ¶ 11.

⁸⁵ *Id.* ¶ 16.

⁸⁶ *Id.* ¶¶ 15, 26.

⁸⁷ *See supra* note 3 and accompanying text.

⁸⁸ Although the 1995 BIT post-dates the 1994 PSI Agreement:

It should be noted that the BIT, by its express terms (Article 2), is made applicable to investments made in the territory of a Contracting Party on 2 September 1954 and onward. Thus disputes arising in respect of investments made as early as 2 September 1954, in other words, pre-BIT disputes, may be brought before an ICSID tribunal constituted pursuant to the BIT [including the present dispute].

Pakistan, ICSID (W. Bank) Case No. ARB/01/13 ¶ 153.

⁸⁹ *Id.* ¶ 35.

(Article 11), which provided: “Either Contracting Party shall constantly guarantee the observance of the commitments it has entered into with respect to the investments of the investors of the other Contracting Party.”⁹⁰

An ICSID Tribunal was duly constituted and it turned first to consider Pakistan’s objections to jurisdiction.⁹¹ Specifically, Pakistan alleged that the claims were essentially contractual in nature and SGS was improperly reformulating them as BIT claims.⁹² Since the PSI Agreement specifically referred any disputes there under to arbitration in Pakistan, Pakistan argued that the ICSID Tribunal lacked jurisdiction to hear SGS’s claim.⁹³

SGS argued, however, that under the umbrella clause in the BIT, *all* contract claims were automatically “elevat[ed]” to BIT claims since Pakistan was obliged under the clause to “constantly guarantee” its investment “commitments” to Swiss investors, which included all contractual commitments.⁹⁴ As such, SGS asserted that the ICSID Tribunal had jurisdiction over the contractual dispute.⁹⁵

1. BIT Provisions Establishing Substantive Standards of Treatment

In considering the scope of its jurisdiction, the Tribunal first considered Article 9 of the BIT, which refers to ICSID arbitration any “disputes with respect to investments between a Contracting Party and an investor of the other Contracting Party. . . .”⁹⁶ While it is broadly rendered, the Tribunal reasoned that

[I]f Article 9 relates to any dispute at all between an investor and a Contracting Party, it must comprehend disputes constituted by claimed violations of BIT provisions establishing substantive standards of treatment by one Contracting Party of investors of the other Contracting Party [since a]ny other view would tend to erode significantly those substantive treaty standards of treatment.⁹⁷

Additionally, because the BIT was concluded after the PSI Agreement, the parties could not have intended to subject disputes under the BIT to the arbitration procedures laid out in the PSI Agreement.⁹⁸ Accordingly, the

⁹⁰ *Id.* ¶¶ 97-99.

⁹¹ *Id.* ¶¶ 43-82.

⁹² *Id.* ¶¶ 43-45.

⁹³ *Id.* ¶¶ 1-3.

⁹⁴ *Pakistan*, ICSID (W. Bank) Case No. ARB/01/13 ¶¶ 53-54, 98-99.

⁹⁵ *Id.* ¶¶ 53-54.

⁹⁶ *Id.* ¶ 149.

⁹⁷ *Id.* ¶ 150.

⁹⁸ *Id.* ¶ 154.

Tribunal determined that it had jurisdiction over those SGS claims premised on BIT provisions establishing substantive standards of treatment⁹⁹ (the “BIT claims”), including BIT Articles 3(1), 4(1)-(2) and 6(1), which relate respectively to the promotion of investments, the protection of investments, and expropriation.¹⁰⁰ Such claims were treaty claims as they were “based not on the PSI Agreement, but rather allege a cause of action under the BIT,”¹⁰¹ it being “for the Claimant to characterize the claims as it sees fit.”¹⁰²

2. Scope of Umbrella Clause Regarding Purely Contractual Obligations

Conversely, the Tribunal determined that it had no jurisdiction over those SGS claims “based on alleged breaches of the PSI Agreement which [did] not also constitute or amount to breaches of the substantive standards of the BIT.”¹⁰³ In so deciding, the Tribunal rejected SGS’s argument that Article 11 of the BIT, the umbrella clause, automatically elevated any and all breaches under the PSI Agreement to BIT violations.¹⁰⁴ Noting that the text of Article 11 “appears susceptible of almost indefinite expansion,”¹⁰⁵ the Tribunal considered the legal consequences attending SGS’s interpretation “so far-reaching in scope, and so automatic and unqualified and sweeping in their operation, so burdensome in their potential impact upon a Contracting Party . . . that clear and convincing evidence must be adduced by the Claimant . . . that such was indeed the shared intent of the Contracting Parties”¹⁰⁶ The Tribunal, however, found no such evidence.¹⁰⁷

Among those legal consequences the Tribunal found far-reaching was that “Article 11 would amount to incorporating by reference an unlimited number of State contracts, as well as other municipal law instruments setting out State commitments to an investor of the other Contract Party,” the

⁹⁹ *Id.* ¶ 150.

¹⁰⁰ *Pakistan*, ICSID (W. Bank) Case No. ARB/01/13 ¶ 96.

¹⁰¹ *See id.* ¶ 154.

¹⁰² *Id.* ¶ 145. The Tribunal also noted that in pleading its case, so long as “the facts asserted by the Claimant are capable of being regarded as alleged breaches of the BIT, consistently with the practice of ICSID tribunals, the Claimant should be able to have them considered on their merits.” *Id.*

¹⁰³ *Société Général de Surveillance S. A. v. Pakistan*, Decision of the Tribunal on Objections to Jurisdiction, ICSID (W. Bank) Case No. ARB/01/13, ¶ 162 (2003), available at <http://www.worldbank.org/icsid/cases/SGS-decision.pdf>.

¹⁰⁴ *Id.* ¶ 163.

¹⁰⁵ *Id.* ¶ 166.

¹⁰⁶ *Id.* ¶ 167.

¹⁰⁷ *Id.* ¶ 173.

alleged violation of which would be treated as a BIT breach.¹⁰⁸ Additionally, BIT Articles 3 to 7,¹⁰⁹ which lay down various substantive treaty standards, would be superfluous if any simple breach of a contract between the parties sufficed to bring the BIT into play.¹¹⁰ A third consequence would have been that an investor could nullify at will any freely negotiated dispute settlement clause in an investor-State contract.¹¹¹ In sum, *SGS v. Pakistan* stands for the proposition that there is a strong presumption that umbrella clauses do not apply to obligations arising under investor-State contracts.

B. *SGS v. Philippines*

Just six months later, however, another ICSID Tribunal, in *SGS v. Philippines*,¹¹² came to a different conclusion in interpreting the umbrella clause in the Switzerland-Philippines BIT, which provides that: “Each Contracting Party shall observe any obligation it has assumed with regard to specific investments in its territory by investors of the other Contracting Party.”¹¹³ At issue was the umbrella clause’s application to a dispute concerning how much the Philippines owed SGS for unpaid comprehensive import supervision services provided under a contract between the parties (the “CISS Agreement”).¹¹⁴ Specifically, the question for the Tribunal was

¹⁰⁸ *Id.* ¶ 168.

¹⁰⁹ Specifically:

[T]he substantive obligations undertaken by the Contracting Parties in Articles 3 to 7 [concern] promotion and admission of investments in accordance with the laws and regulations of the Contracting Party (Article 3); prohibition of impairment, by ‘unreasonable or discriminating measures,’ of the management, use, enjoyment, *etc.* of such investments and according ‘fair and equitable treatment’ to investors of the other Contracting Party (Article 4); free cross-border transfer of payments relating to the protected investments (Article 5); prohibition of expropriation or other measures having the same nature or effect, unless taken in the public interest, on a non-discriminatory basis, under due process of law and with provision for effective and adequate and prompt compensation (Article 6); and the most-favored-investor provision (Article 7).

Pakistan, ICSID (W. Bank) Case No. ARB/01/13 ¶ 169.

¹¹⁰ *Id.* ¶ 168.

¹¹¹ *Id.* ¶ 168. Apart from these consequences, the Tribunal also based its decision on the fact that Article 11 was not placed in the same section of the BIT as Articles 3 to 7. Its separate location indicated to the Tribunal that Article 11 was not meant to embody a “substantive ‘first order’ obligation” like those in Articles 3 to 7, much less supersede those provisions. *Id.* ¶ 170.

¹¹² *Société Général de Surveillance S. A. v. Philippines*, Decision of the Tribunal on Objections to Jurisdiction, ICSID (W. Bank) Case No. ARB/02/6 (2004), *reprinted in* 19 MEALEY’S INT’L. ARB. REP. 6 (2004).

¹¹³ *Id.* ¶ 34.

¹¹⁴ *See id.* ¶¶ 1, 12-17. The comprehensive import supervision services provided by SGS to Philippines are similar in nature to the services provided by SGS to Pakistan. *Id.* ¶ 95.

whether it had jurisdiction over claims concerning CISS Agreement breaches by virtue of the umbrella clause.¹¹⁵

1. Scope of Umbrella Clause

Looking to the text of the umbrella clause, the Tribunal noted that in providing for “any obligation” concerning investment between the parties, the umbrella clause could readily be interpreted to include any obligation that arises from a contract between the parties.¹¹⁶ Such an inclusive reading of the clause was further consistent with the BIT’s purpose, which was “to create and maintain favourable conditions for investments . . .”¹¹⁷ Accordingly, the Tribunal determined that it had jurisdiction over claims arising under the CISS Agreement since the umbrella clause, properly construed, “makes it a breach of the BIT for the host State to fail to observe binding commitments, including contractual commitments, which it has assumed with regard to specific investments.”¹¹⁸

In determining that the umbrella clause applied to investor-State contracts, the Tribunal explicitly rejected the underlying rationale of the *SGS v. Pakistan* decision.¹¹⁹ While acknowledging that the umbrella clause’s wording was more vague in requiring a party to “*constantly guarantee* the observance of . . . commitments”¹²⁰ (as compared with Article X(2) of the Switzerland-Philippines BIT, which called for parties to “observe any obligations”),¹²¹ the Tribunal nonetheless considered the earlier decision to have given the umbrella clause “a highly restrictive interpretation” that was not justified by the rationales proffered.¹²²

The Tribunal took issue with the earlier decision’s criticism of the interpretation favored by SGS as over-reaching in possibly encompassing all

¹¹⁵ *Id.* ¶ 92(b).

¹¹⁶ *See id.* ¶ 115.

¹¹⁷ *Philippines*, ICSID (W. Bank) Case No. ARB/02/6 ¶ 116 (internal quotations omitted); *see also id.* ¶ 117 (“[I]f commitments made by the State towards specific investments do involve binding obligations or commitments under the applicable law, it seems entirely consistent with the object and purpose of the BIT to hold that they are incorporated and brought within the framework of the BIT by Article X(2).”).

¹¹⁸ *Id.* ¶ 128.

¹¹⁹ *Id.* ¶¶ 119-26.

¹²⁰ *Id.* ¶ 119 (emphasis added) (quoting Agreement between the Swiss Confederation and the Islamic Republic of Pakistan on the Promotion and Reciprocal Protection of Investments, Switz.-Pak., art. 11, Jul. 11, 1995, available at http://www.unctad.org/sections/dite/ia/docs/bits/switzerland_pakistan_fr.pdf).

¹²¹ *Id.* ¶ 115.

¹²² *Philippines*, ICSID (W. Bank) Case No. ARB/02/6 ¶ 120.

manner of State actions.¹²³ Noting that the umbrella clause was in fact limited to “obligations assumed with regard to specific investments,” the Tribunal pointed out that for it to be applicable:

[T]he host State must have assumed a legal obligation, and it must have been assumed vis-à-vis the specific investment-not as a matter of the application of some legal obligation of a general character. This is very far from elevating to the international level all the ‘municipal legislative or administrative or other unilateral measures of a Contracting Party.’¹²⁴

The Tribunal also rejected the prior decision’s characterization of a broad interpretation of the umbrella clause as involving a full-scale internationalization of domestic contracts whereby all investment contracts are immediately “transubstanti[ated]” into treaties.¹²⁵ According to the Tribunal, an umbrella clause “does not convert questions of contract law into questions of treaty law,” or more specifically in the case before it, Article X(2) “does not change the proper law of the CISS Agreement from the law of the Philippines to international law.”¹²⁶ Rather, the umbrella clause “addresses not the *scope* of the commitments entered into with regard to specific investments but the *performance* of these obligations, once they are ascertained.”¹²⁷

Not only did the Tribunal find unconvincing the rationales provided in *SGS v. Pakistan*, it faulted the decision for failing to give any clear meaning to the umbrella clause.¹²⁸ Relevantly, the earlier decision stated that the umbrella clause signaled “an implied affirmative commitment to enact implementing rules . . . appropriate to give effect to a contractual or statutory undertaking in favor of investors” and that it did not preclude the possibility that under “exceptional circumstances,” certain breaches of contract might constitute BIT violations.¹²⁹ Yet, as the Tribunal noted, “[the umbrella clause,] if it has any effect at all, confers jurisdiction on an international tribunal, and needs to do so with adequate certainty. Jurisdiction is

¹²³ *Id.* ¶ 121.

¹²⁴ *Id.* ¶ 121 (quoting *Société Générale de Surveillance S. A. v. Pakistan*, Decision of the Tribunal on Objections to Jurisdiction, ICSID (W. Bank) Case No. ARB/01/13, ¶ 166 (2003), available at <http://www.worldbank.org/icsid/cases/SGS-decision.pdf>).

¹²⁵ *See id.* ¶ 126 (quoting *Pakistan*, ICSID Case No. ARB/01/13 ¶ 172).

¹²⁶ *Id.* ¶ 126.

¹²⁷ *Id.* (emphasis in original).

¹²⁸ *Philippines*, ICSID (W. Bank) Case No. ARB/02/6 ¶ 125. The Tribunal also questioned the finding in *SGS v. Pakistan* that the umbrella clause’s location at the end of the BIT (as opposed to the part of the text that laid out substantive obligations) supported its restrictive interpretation. As the Tribunal noted, the umbrella clause must surely have *some* meaning, and the Tribunal found it “difficult to accept that . . . it is legally inoperative . . . merely because of its location.” *Id.* ¶ 124.

¹²⁹ *Pakistan*, ICSID (W. Bank) Case No. ARB/01/13 ¶ 172.

not conferred by way of ‘an implied affirmative commitment’ or through the characterization of circumstances as ‘exceptional.’”¹³⁰

Thus, contrary to the decision in *SGS v. Pakistan*, the Tribunal in *SGS v. Philippines* decided that the umbrella clause applies to all breaches of the relevant investor-State contract.¹³¹ The Tribunal, therefore, had jurisdiction over contractual disputes arising under the CISS Agreement, including any purely contractual claims that were not also premised on the BIT’s substantive provisions.¹³² However, even though the Tribunal found that it had jurisdiction over SGS’s contractual claims, the Tribunal ultimately declined to exercise such jurisdiction on the ground that it was inappropriate to do so in this case since the Agreement contained an exclusive forum selection clause that designated a different forum for resolving such contractual disputes.¹³³

2. Effect of Forum Selection Clause in Contract

Article 12 of the CISS Agreement provided that the agreement was to be “governed in all respects by . . . the laws of the Philippines” and that “[a]ll actions concerning disputes in connection with the obligations of either party to this Agreement shall be filed at the Regional Trial Courts of Makati or Manila.”¹³⁴ In contrast, BIT Article VIII provided the investor with a choice of “submit[ting any disputes with respect to investments between a Contracting Party and an investor of the other Contracting Party] either to the national jurisdiction of the Contracting Party in whose territory the investment has been made or to international arbitration [under ICSID or UNCITRAL].”¹³⁵

In declining to exercise jurisdiction over the contractual disputes, a majority of the Tribunal rejected SGS’s argument that the Switzerland-Pakistan BIT overrode the contract’s forum selection clause.¹³⁶ Applying

¹³⁰ *Philippines*, ICSID (W. Bank) Case No. ARB/02/6 ¶ 125.

¹³¹ *See id.* ¶¶ 113-28.

¹³² *Id.* ¶ 169(3) (concluding that “[u]nder Article VIII(2) of the BIT, the Tribunal has jurisdiction with respect to a claim arising under the CISS Agreement, even though it may not involve any breach of the substantive standards of the BIT”).

¹³³ *Id.* ¶ 155.

¹³⁴ *Id.* ¶ 22.

¹³⁵ *Id.* ¶ 34.

¹³⁶ *Philippines*, ICSID (W. Bank) Case No. ARB/02/6 ¶¶ 140-41. The sole dissenter, Antonio Crivellaro, specifically disagreed with the majority’s decision to stay the proceedings but otherwise joined the Tribunal in the decision. *See generally* Société Général de Surveillance S. A. v. Philippines, Decision by One of the Arbitrators (“Crivellaro Declaration”), ICSID (W. Bank) Case No. ARB/02/6 (2004), available at <http://www.worldbank.org/icsid/cases/SGSvPhil-declaration.pdf>.

the maxim *generalia specialibus non derogant*, the majority found that the CISS Agreement's forum selection clause should be given precedence over the BIT since the former applied more specifically to the dispute at hand.¹³⁷ According to the majority, the forum selection clause applied only to disputes arising out of the CISS Agreement, whereas the BIT, while applicable to the CISS Agreement, "was not concluded with any specific investment or contract in view" and was also potentially applicable to multiple investment arrangements involving other parties.¹³⁸

The majority further stated that a BIT is intended by the State parties to support and complement, rather than displace, the specific negotiated investment arrangements between the investor and the host State.¹³⁹ As such, the majority regarded it inconsistent with the BIT's purpose to construe it as overriding an exclusive forum selection clause in the underlying contract.¹⁴⁰

In his dissent, which he specifically limited to the Tribunal's decision to stay its proceedings, Antonio Crivellaro disagreed with the majority's assessment that the BIT provision overrode the contractual forum selection clause.¹⁴¹ Since the BIT was entered into only after the CISS Agreement was concluded, SGS could not possibly have waived its right to rely on the BIT's dispute resolution provisions when it agreed to refer contractual disputes to the courts of the Philippines under the CISS Agreement.¹⁴² Rather, "the BIT has created a completely new law and has conferred on SGS new or additional rights of forum selection . . . includ[ing], in particular the right to select the forum *after the dispute has arisen*."¹⁴³ Additionally, given that a central, if not the most important, advantage afforded to investors under the BIT is their right to a choice of forums under the BIT's dispute resolution provisions,¹⁴⁴ as between conflicting dispute resolution provisions, "the rule giving prevalence to the most favourable treatment [to its beneficiary] certainly applies."¹⁴⁵

The majority did not, however, address the arguments in the dissent, except to note indirectly that the dissent's conclusion meant that a different answer arises depending on whether the BIT predated or postdated the relevant contract.¹⁴⁶ Instead, the majority pointed to another finding to support

¹³⁷ *Philippines*, ICSID (W. Bank) Case No. ARB/02/6 ¶ 141.

¹³⁸ *Id.*

¹³⁹ *Id.*

¹⁴⁰ *See id.* ¶¶ 132, 141.

¹⁴¹ *Crivellaro Declaration*, ICSID (W. Bank) Case No. ARB/02/6 ¶ 4.

¹⁴² *Id.* ¶ 2.

¹⁴³ *Id.* (emphasis in original).

¹⁴⁴ *Id.* ¶ 3.

¹⁴⁵ *Id.* ¶ 10.

¹⁴⁶ *Philippines*, ICSID (W. Bank) Case No. ARB/02/6 ¶ 141 n.70.

its conclusion, to wit: In bringing its claim, SGS was relying on the very contract whose forum selection clause it had deliberately disregarded. The majority noted that:

[W]here a claimant has expressly agreed in writing . . . that in all matters pertaining to the execution, fulfillment, and interpretation of the contract he will have resort to local tribunals, remedies, and authorities, and then willfully ignores them by applying in such matters [for remedies under broadly applicable treaties], he will be held bound by his contract.¹⁴⁷

Put differently, “a party to a contract cannot claim on that contract without itself complying with it.”¹⁴⁸ SGS was thus not permitted to “appropriate and reprobate in respect of the same contract,” but must bring any claims under the CISS Agreement to the Philippines’ courts.¹⁴⁹

Finally, the majority also made clear that its refusal to decide the dispute was an issue that went to the admissibility of the claim and not jurisdiction for “unless otherwise expressly provided, treaty jurisdiction is not abrogated by contract.”¹⁵⁰ That is, the majority determined that the Tribunal had jurisdiction over the dispute, but regarded SGS’s claim to be inadmissible on account of the forum selection clause in the CISS Agreement, which required SGS to submit the dispute to the Philippines courts.¹⁵¹

Significantly, such a characterization meant that the Tribunal might yet have to resolve the claim if, for example, the Philippines courts were unable or unwilling to resolve the dispute.¹⁵² The majority described its situation as one where “Philippines’ responsibility under Article X(2) and IV of the BIT—a matter which does fall under its jurisdiction—is subject to ‘the factual predicate of a determination’ by the Regional Trial Court of [SGS’s claim].”¹⁵³

Under these circumstances, the Tribunal decided to stay the proceedings pending a resolution of the dispute by the Philippines court or through agreement of the parties.¹⁵⁴ Declaring that the stay of proceedings may be lifted “for sufficient cause on application by either party,” the Tribunal or-

¹⁴⁷ *Id.* ¶ 151 (quoting The United States-Venezuela Claims Protocol, U.S.-Venez., Feb. 17, 1903, 101 B.F.S.P. 646, 2 Malloy 1870) (1903)).

¹⁴⁸ *Id.* ¶ 154.

¹⁴⁹ *Id.* ¶ 155.

¹⁵⁰ *Id.* ¶ 154.

¹⁵¹ *Id.* ¶¶ 154-55.

¹⁵² *Philippines*, ICSID (W. Bank) Case No. ARB/02/6 ¶ 170 (noting that “a party could not be required to litigate locally if the local courts are closed to it due to armed conflict.”).

¹⁵³ *Id.* ¶ 174.

¹⁵⁴ *Id.* ¶ 175.

dered the parties to appraise it every six months on the status of the claim.¹⁵⁵

Thus, the Tribunal in *SGS v. Philippines* determined that while the umbrella clause extends in theory to all breaches of contract, it does not override any exclusive forum selection clause in the contract and should not be applied where the latter designates a forum other than that provided under the BIT.

C. *Decisions in the Wake of the SGS Cases*

A number of international arbitration decisions following the *SGS* cases have also addressed the umbrella clause, though not always with the same level of detail. As a group, these decisions advance a broader and more inclusive interpretation of the umbrella clause, and in that respect, are closer to *SGS v. Philippines* than *SGS v. Pakistan*.¹⁵⁶ However, they do not speak with one voice on the question.¹⁵⁷ For instance, certain cases limit the application of the umbrella clause to some but not all contractual obligations,¹⁵⁸ demonstrating vividly the prevailing uncertainty in the wake of the *SGS* cases.¹⁵⁹

A case in point is *Joy Mining v. Egypt*.¹⁶⁰ The Tribunal there examined Article 2(2) of the Egypt-United Kingdom BIT, which provides in relevant part that: “Each Contracting Party shall observe any obligation it may have entered into with regard to investments of nationals or companies of the other Contracting Party.”¹⁶¹

¹⁵⁵ *Id.* ¶ 176.

¹⁵⁶ See Katia Yannaca-Small, *Working Paper on International Investment, No. 2006/1: Improving the System of Investor-State Dispute Settlement: An Overview*, ¶ 132 (OECD, Working Paper No. 2006/1, 2006) (noting in its review of cases considering the umbrella clause that “there is a growing consistency on the interpretation of [the umbrella clause’s] meaning to include ‘all obligations’ by the State, both treaty and contractual”).

¹⁵⁷ See *id.* (noting that notwithstanding “growing consistency” on the question, “the decisions . . . do not all reach the same conclusion on the interpretation of the ‘umbrella clause’”).

¹⁵⁸ See, e.g., *infra* text accompanying notes 160-66.

¹⁵⁹ Additionally, while the decisions following the *SGS* cases examine the question concerning whether and to what extent the umbrella clause extends to contractual obligations, they do not appear to discuss in any meaningful way the question raised in *SGS v. Philippines* on whether an umbrella clause should apply in the presence of an exclusive forum selection clause in the contract.

¹⁶⁰ See *Joy Mining Mach. Ltd. v. Egypt*, Award on Jurisdiction, ICSID (W. Bank) Case No. ARB/03/11 (2004), available at <http://www.worldbank.org/icsid/cases/joy-mining-award.pdf>.

¹⁶¹ See Christoph Schreuer, *Investment Treaty Arbitration and Jurisdiction Over Contract Claims—the Vivendi Case Considered*, in *INTERNATIONAL INVESTMENT LAW AND ARBITRATION* 281, 301 (Todd Weiler ed., 2005) (quoting Agreement for the Promotion and Protection of Investments, Egypt-U.K., art.2, June 11, 1975, available at http://www.unctad.org/sections/dite/ia/docs/bits/egypt_

After declaring that it was not pronouncing judgment on the views of other tribunals including those in the *SGS* cases, the Tribunal noted in dicta its view of the umbrella clause as follows:

In this context, it could not be held that an umbrella clause inserted in the Treaty, and not very prominently, could have the effect of transforming all contract disputes into investment disputes under the Treaty, unless of course there would be a clear violation of the Treaty rights and obligations or a violation of contract rights of such a magnitude as to trigger the Treaty protection, which is not the case. The connection between the Contract and the Treaty is the missing link that prevents any such effect. This might be perfectly different in other cases where that link is found to exist, but certainly it is not the case here.¹⁶²

Similarly, the ICSID Tribunal in *CMS v. Argentina* found that the umbrella clause applied to some but not all contractual obligations.¹⁶³ In that case, the Tribunal had to consider the effect of Article II(2)(c) of the Argentina-United States BIT, which provides that each party “shall observe any obligation it may have entered into with regard to investments.”¹⁶⁴ Claiming to rely *inter alia* on the *SGS* cases and *Joy Mining v. Egypt*, the Tribunal determined that the umbrella clause distinguished between “commercial disputes” and those “disputes arising from the breach of treaty standards and their respective causes of action.”¹⁶⁵ According to the Tribunal, the umbrella clause applied only to the latter, which “likely” included situations involving “significant interference by government or public agencies with the rights of the investors.”¹⁶⁶

In contrast to *Joy Mining* and *CMS*, however, other decisions have observed more generally that the umbrella clause extends to contractual obligations without excluding particular categories of contractual obligations from its scope. For example, the Tribunal in *Consortio Groupement*

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¹⁶² *Joy Mining*, ICSID (W. Bank) Case No. ARB/03/11 ¶ 81. The Tribunal acknowledged earlier in the Award that its conclusion that it lacked jurisdiction over the dispute, which fell outside the BIT, “would render it unnecessary to discuss the other jurisdictional objections and issues raised by the Respondent.” *Id.* ¶ 63. Unfortunately for the already confused state of the law, it proceeded nonetheless to consider *inter alia* the issue of umbrella clauses for the asserted purpose of “mak[ing] certain clarifications concerning the nature of the Contract and the role of the forum selection clause contained therein.” *Id.* As Schreuer points out, however, to require an independent treaty violation under the umbrella clause is to negate its effect, and the reference to the “missing link” is incomprehensible and quite far from amounting to a clarification. See Schreuer, *supra* note 161, at 301.

¹⁶³ See *CMS Gas Transmission Co. v. Argentine Republic*, Award, ICSID (W. Bank) Case No. ARB/01/8, ¶¶ 299-301 (2005).

¹⁶⁴ *Id.* ¶ 296.

¹⁶⁵ *Id.* ¶ 300.

¹⁶⁶ *Id.* ¶ 299.

L.E.S.I.-DIPENTA v. Algeria stated that “the effect of [umbrella] clauses is to transform the violations of the State’s contractual commitments into violations of the treaty umbrella clause and by this to give jurisdiction to the Tribunal over the matter”¹⁶⁷ Indeed, at least one decision has held that when the umbrella clause is phrased in the imperative—which, incidentally, was the case in both *Joy Mining* and *CMS*—it must be held to apply without exception to all contractual obligations.¹⁶⁸ In *Eureko B.V. v. Poland*, the Tribunal commented thus on the umbrella clause in the Netherlands-Poland BIT:

The plain meaning—the ‘ordinary meaning’—of a provision prescribing that a State ‘shall observe any obligations it may have entered into’ with regard to certain foreign investments is not obscure. The phrase ‘shall observe’ is imperative and categorical. ‘Any’ obligations is capacious [sic]; it means not only obligations of a certain type, but ‘any’—that is to say, all—obligations entered into with regard to investments of investors of the other Contracting Party.¹⁶⁹

Other decisions, however, while agreeing that the umbrella clause applies in general to contractual obligations, have stopped short of holding that it applies without exception to all such obligations. In *Noble Ventures, Inc. v. Romania*,¹⁷⁰ the Tribunal examined the umbrella clause in the United States-Romania BIT, which provides that “[e]ach Party shall observe any obligation it may have entered into with regard to investments.”¹⁷¹ Although the Tribunal acknowledged that the wording of the umbrella clause was “a clear reference to investment contracts,”¹⁷² it declined “to express any definitive conclusion as to whether . . . [the umbrella clause] perfectly assimilates to breach of the BIT *any* breach by the host State of *any* contractual obligation” on the ground that its conclusions in that case would not be affected by the resolution of that question.¹⁷³

¹⁶⁷ Yannaca-Small, *supra* note 156, ¶ 127 (quoting Consorzio Groupement L.E.S.I.-DIPENTA v. The Republic of Algeria, Award, ICSID (W. Bank) Case No. ARB/03/08, ¶ 25(ii) (2005), as translated by the Secretariat). *See also* Waste Mgmtl, Inc. v. United Mexican States, Arbitral Award, ICSID (W. Bank) Case No. ARB (AF)/00/3, ¶ 73 (2004) *available at* http://www.economia-snci.gob.mx/sphp_page/s/importa/sol_contro/consultoria/Casos_Mexico/Waste_2_management/laudo/laudo_ingles.pdf (noting in dicta that “an ‘umbrella clause’ commit[s] the host State to comply with its contractual commitments”).

¹⁶⁸ *Eureko B.V. v. Poland*, Partial Award on Liability, ¶ 246 (*ad hoc* arbitration of Aug. 19, 2005), *available at* <http://www.investmentclaims.com/decisions/Eureko-Poland-LiabilityAward.pdf>.

¹⁶⁹ *Id.*

¹⁷⁰ *Noble Ventures, Inc. v. Romania*, Award, ICSID (W. Bank) Case No. ARB/01/11 (2005), *available at* <http://ita.law.uvic.ca/documents/Noble.pdf>.

¹⁷¹ *Id.* ¶ 46.

¹⁷² *Id.* ¶ 51.

¹⁷³ *Id.* ¶ 61 (emphasis in original).

Much more ambiguous is the decision of *Sempra Energy International v. Argentina*.¹⁷⁴ In that case, the Tribunal noted that the dispute before it arose from the manner in which “the violation of contractual commitments with the [claimant] licensees, expressed in the license and other acts, impacts the rights the investor claims to have in the light of the provisions of the treaty and the guarantees on the basis of which it made the protected investment.”¹⁷⁵ It then went on to hold that it had jurisdiction over the investor’s claim since it was “founded on both the contract and the [BIT]” and “[t]he fact that the [BIT] also includes the specific guarantee of a general ‘umbrella clause,’ . . . involving the obligation to observe contractual commitments concerning the investment, creates an even closer link between the contract, the context of the investment and the Treaty.”¹⁷⁶ Because the Tribunal did not specify which BIT provisions it regarded the claims to be premised upon, it is not entirely clear whether the Tribunal would have found jurisdiction over purely contractual claims by virtue of the umbrella clause, let alone over all contractual claims.

Thus, while the decisions following the *SGS* cases adopt in general a more expansive reading of the umbrella clause’s scope, they do not agree on whether it extends to every contractual obligation. As the discussion below illustrates, however, the language and purpose of the umbrella clause, as informed by its history, reveals that the more reasonable interpretation is that the umbrella clause extends to all obligations arising under any investment contract between a State party to the BIT and an investor of the other State party.

IV. DISCUSSION

Following the divergent decisions in the two *SGS* cases, the question that has emerged in the debate over umbrella clauses is two-fold: (1) whether any and all breaches of investor-State contracts are also BIT violations under the umbrella clause, and if so; (2) whether the BIT tribunal may exercise jurisdiction over claims concerning breaches of contract notwithstanding any exclusive forum selection clause in the contract designating a different forum for the resolution of disputes.

¹⁷⁴ *Sempra Energy Int’l v. Argentine Republic*, Decision of the Tribunal on Objections to Jurisdiction, ICSID (W. Bank) Case No. ARB/02/16 (2005).

¹⁷⁵ *Id.* ¶ 100.

¹⁷⁶ *Id.* ¶ 101.

A. *The Scope of the Umbrella Clause In Relation to Contractual Disputes*

On the question of whether umbrella clause applies to all breaches of contract, the approach adopted in *SGS v. Philippines* is eminently preferable to that in *SGS v. Pakistan*. As pointed out in the former decision, the natural interpretation of a broadly-worded umbrella clause referring simply to “obligations” is that it includes contractual obligations, a reading further supported by the BIT’s purpose of encouraging investments.¹⁷⁷ This also accords with well-established standards of interpreting treaties under international law as laid out in the Vienna Convention of the Law of the Treaties, which provides that “[a] treaty shall be interpreted in good faith in accordance with the *ordinary meaning* to be given to the terms of the treaty in their context and in the light of its object and purpose.”¹⁷⁸

In referring without qualification to investment “obligations,” the “ordinary meaning” of that term indubitably includes contractual obligations. Indeed, since previous ICSID cases dealing with *pre-contractual* claims have determined that no investment is made until a contract is concluded,¹⁷⁹ and since umbrella clauses apply only to obligations regarding *investment*, the umbrella clause simply has no “clear meaning” if contractual obligations are excluded from its scope.¹⁸⁰ To paraphrase the *SGS v. Pakistan* Tribunal’s interpretation of Article 9 (the forum selection clause) of the Switzerland-Pakistan BIT, if the umbrella clause relates to any obligations between an investor and a Contracting Party, it must comprehend those obli-

¹⁷⁷ See *supra* Part III.B.1.

¹⁷⁸ Vienna Convention on the Law of Treaties, art. 31, *opened for signature* May 23, 1969, 1155 U.N.T.S. 331 (emphasis added), *reprinted in* 8 I.L.M. 679 (1969). See also *Eureko B.V. v. Poland*, Partial Award on Liability, ¶¶ 246-7 (*ad hoc* arbitration of Aug. 19, 2005), *available at* <http://www.investmentclaims.com/decisions/Eureko-Poland-LiabilityAward.pdf> (basing its interpretation of a BIT on the “authoritative codification the law of treaties [that] is the Vienna Convention on the Law of Treaties” and noting that the “ordinary meaning” of obligations includes contractual obligations).

¹⁷⁹ See, e.g., *Mihaly Int’l Corp. v. Sri Lanka*, Award, ICSID (W. Bank) Case No. ARB/00/2, ¶¶ 48, 51 (2002), *available at* <http://www.worldbank.org/icsid/cases/mihaly-award.pdf> (holding that pre-contractual expenses incurred do not amount to an investment).

¹⁸⁰ *Société Général de Surveillance S. A. v. Philippines*, Decision of the Tribunal on Objections to Jurisdiction, ICSID (W. Bank) Case No. ARB/02/6, ¶ 125 (2004), *reprinted in* 19 MEALEY’S INT’L. ARB. REP. 6 (2004). It might be argued, however, that the umbrella clauses could have been designed rather to apply exclusively to such precontractual obligations. This argument has the perverse effect, however, of greatly broadening the effect of the umbrella clause and the BIT when such a consequence was precisely that relied on in *SGS v. Pakistan* for refusing to extend umbrella clauses to investor-State contracts. See *supra* Part III.A.2. In any event, nothing in the history of the umbrella clause would appear to support such an interpretation. See *supra* Part II.

gations arising in a contract between them since any other view would erode significantly the meaning of an umbrella clause.¹⁸¹

The Tribunal in *SGS v. Pakistan* turned this issue on its head, however, in rejecting SGS's interpretation of the umbrella clause on the ground that it rendered superfluous *other substantive standards of treatment prescribed in the treaty* since the BIT could be invoked by a mere breach of contract.¹⁸² Yet, this reasoning is erroneous since such substantive provisions of the BIT encompass standards that are not typically addressed in contracts, including fair and equitable treatment, "most-favored-nation" status, non-discrimination, and protection from expropriation.¹⁸³ Conveniently, the Tribunal in *SGS v. Pakistan* also failed to articulate what the umbrella clause applied to if not contractual obligations.¹⁸⁴ It was thus content for the clause to be superfluous even as it complained about other provisions being made redundant.

Even assuming the meaning of "obligations" or "commitments" is ambiguous, prior commentary on the umbrella clause's effects and its history support the more inclusive interpretation adopted in *SGS v. Philippines*.¹⁸⁵ As described above, the extended history of the umbrella clause demonstrates that it was specifically intended to apply to investor-State contracts, and was designed to overcome the presumption that a breach of contract did not engage international responsibility.¹⁸⁶

Additionally, the one ICSID decision that touched on the issue before either of the *SGS* cases, *Fedax v. Venezuela*,¹⁸⁷ also concluded that a State's breach of a contractual obligation owed to an investor constituted a BIT violation.¹⁸⁸ In that case, Venezuela failed to honor certain promissory notes it had issued, and the respondent sought recovery under the Netherlands-Venezuela BIT.¹⁸⁹ Article 3 of the BIT was an umbrella clause requiring each State to "observe any obligation it may have entered into with regard

¹⁸¹ See *supra* text accompanying note 97 (quoting Société Général de Surveillance S. A. v. Pakistan, Decision of the Tribunal on Objections to Jurisdiction, ICSID (W. Bank) Case No. ARB/01/13, ¶150 (2003), available at <http://www.worldbank.org/icsid/cases/SGS-decision.pdf>).

¹⁸² See *supra* Part III.A.2.

¹⁸³ See Schreuer, *supra* note 3, at 253 ("The BIT's substantive provisions deal with . . . issues . . . not normally covered in contracts. Therefore, extending the BIT's protection to investment contracts would not make the substance of a BIT superfluous.").

¹⁸⁴ See *Philippines*, ICSID (W. Bank) Case No. ARB/02/6 ¶ 125 (noting that "the [*SGS v. Pakistan*] Tribunal failed to give any clear meaning to the 'umbrella clause'").

¹⁸⁵ See *supra* Part II.

¹⁸⁶ *Id.*

¹⁸⁷ *Fedax N.V. v. Venezuela*, Award, ICSID (W. Bank) Case No. ARB/96/3 (1998), reprinted in 37 I.L.M. 1391 (1998).

¹⁸⁸ *Id.* ¶ 29.

¹⁸⁹ *Id.* ¶¶ 1, 26.

to the treatment of investments of nationals of the other Contracting Party,” and Article 9(1) and (3) of the BIT limited investor-State arbitration to disputes over obligations under the BIT.¹⁹⁰ While it did not address the umbrella clause directly, the Tribunal determined that Venezuela’s failure to meet its obligations under the promissory notes amounted to a BIT violation:

. . . Venezuela is under the obligation to honor precisely the terms and conditions governing such investment, laid down mainly in [the umbrella clause of the BIT], as well as to honor the specific payments established in the promissory notes issued, and the Tribunal so finds in the terms of Article 9(3) of the [BIT].¹⁹¹

In sum, contrary to the decision in *SGS v. Pakistan*, the proper interpretation of the umbrella clause consistent with its unqualified language, history and prior commentary is that it extends to all breaches of investor-State contracts relating to investments. The first question in our two-part inquiry on umbrella clauses thus answered, we now consider the more challenging but less explored question of the effect of an exclusive forum selection clause in the contract on the application of umbrella clauses.¹⁹²

B. *Exercising Jurisdiction Under the BIT Notwithstanding an Exclusive Forum Selection Clause in the Contract*

While the Tribunal in *SGS v. Philippines* determined that it had jurisdiction over SGS’s contractual dispute by virtue of the umbrella clause, it nevertheless found it inappropriate to exercise such jurisdiction in view of the exclusive forum selection clause in the contract. But this is to take away with one hand what was given with the other, leaving investors no less

¹⁹⁰ Agreement on Encouragement and Reciprocal Protection of Investments, Neth.-Venez., Oct. 22, 1991, 1788 U.N.T.S. 70; see Schreuer, *supra* note 3, at 252; see also *Venezuela*. ICSID (W. Bank) Case No. ARB/96/3 ¶ 30.

¹⁹¹ *Venezuela*, ICSID (W. Bank) Case No. ARB/96/3 ¶ 29.

¹⁹² While commentary following the *SGS* decisions takes the Tribunal in *SGS v. Pakistan* to task for its decision in some detail, see, e.g., Alexandrov, *supra* note 6, at 569-72, Gill et al., *supra* note 33, at 411-2, Schreuer, *supra* note 3, at 254-255, it does not much analyze, if at all, the decision of the Tribunal in *SGS v. Philippines* to stay its proceeding. See Alexandrov, *supra* note 6, at 575 n.119 (noting in a footnote that the BIT did not give SGS an alternative route for the resolution of its contractual dispute in *SGS v. Philippines* even though the tribunal determined that it had jurisdiction over the claims because the forum selection clause in the contract prevailed over the BIT’s jurisdictional clause); Gill et al., *supra* note 33 (no discussion of the issue); Schreuer, *supra* note 3 (same). *But cf.* Emmanuel Gaillard, *Investment Treaty Arbitration and Jurisdiction Over Contract Claims—the SGS Cases Considered*, in INTERNATIONAL INVESTMENT LAW AND ARBITRATION 334, 344-45 (Todd Weiler ed., 2005) (discussing problems associated with the stay decision).

empty-handed than they were under *SGS v. Pakistan*. Indeed, as discussed below, the Tribunal's approach in *SGS v. Philippines* is not only untenable in practice for effectively rendering the umbrella clause a nullity and creating other practical difficulties, it is also misguided in theory for failing to comprehend the relationship between breaches of contract and treaty violations under an umbrella clause. The Tribunal also failed to apply the correct principles of contractual interpretation in resolving the conflict between umbrella clauses and forum selection clauses in contracts. The better interpretation of the umbrella clause allows for its application notwithstanding contractual forum selection clauses.

1. The Tribunal's Approach in Practice

a. *A Superfluous Umbrella Clause*

As its history shows, the umbrella clause was specifically designed to ensure that disputes under investor-State contracts would be resolved in a neutral forum and enforced as a matter of international law.¹⁹³ Notably, in supporting its determination that the umbrella clause includes contractual obligations, the Tribunal in *SGS v. Philippines* stated that the umbrella clause "addresses . . . [and provides] assurances to foreign investors with regard to the *performance* of obligations assumed . . . with regard to specific investments—in effect, to help secure the rule of law in relation to investment protection."¹⁹⁴ This ties in with the fact that a core, if not the most significant, advantage afforded to investors under the BIT is their right to resolve relevant investment disputes with the host State in accordance with the BIT's dispute settlement provisions.¹⁹⁵

Notwithstanding its earlier determination, however, the Tribunal concluded that an umbrella clause in a BIT does not override, and is thus inoperative in the presence of an exclusive forum selection clause in a contract. What this means, however, is that under the Tribunal's interpretation, the umbrella clause will only have effect in one of two scenarios: (a) where the contract's forum selection clause designates the same forum as the BIT; and (b) where the contract does not contain a forum selection clause. Yet,

¹⁹³ See *supra* Part II.

¹⁹⁴ Société Général de Surveillance S. A. v. Philippines, Decision of the Tribunal on Objections to Jurisdiction, ICSID (W. Bank) Case No. ARB/02/6, ¶ 126 (2004), reprinted in 19 MEALEY'S INT'L. ARB. REP. 6 (2004) (second emphasis added).

¹⁹⁵ See Société Général de Surveillance S. A. v. Philippines, Decision by One of the Arbitrators ("Crivellaro Declaration"), ICSID (W. Bank) Case No. ARB/02/6, ¶¶ 5-6 (2004), available at <http://www.worldbank.org/icsid/cases/SGSvPhil-declaration.pdf>.

the umbrella clause is redundant in the first scenario, and the second scenario occurs only infrequently since many if not most investment contracts provide for the resolution of disputes.¹⁹⁶

All of which is to leave the umbrella clause with practically nothing to do. Nor are these consequences ameliorated in any way by the Tribunal's characterization of the issue as one going to admissibility rather than jurisdiction. In finding without exercising jurisdiction, but nonetheless staying the proceedings pending a determination by the Philippines' courts of "the scope or extent of the Respondent's obligation" under the contract,¹⁹⁷ it is not clear what, if anything, is left for the Tribunal to resolve in such an arrangement. As one commentator complained, the decision "results in the BIT tribunal having jurisdiction over an empty shell and depriv[es] the BIT dispute resolution provision of any meaning."¹⁹⁸

Thus, the Tribunal's criticism of the interpretation in *SGS v. Pakistan* as superfluous is equally applicable to its own, namely that it "failed to give any clear meaning to the 'umbrella clause.'"¹⁹⁹ To quote the Tribunal, the umbrella clause "if it has any effect at all"—not to mention some teeth—"confers jurisdiction on an international tribunal, and needs to do so with adequate certainty."²⁰⁰

b. *Problems Associated with Staying the Proceedings*

The Tribunal's approach of staying its proceedings also raises other intractable problems. For example, it is not clear under what circumstances

¹⁹⁶ See Hannah L. Buxbaum, *Forum Selection in International Contract Litigation: The Role of Judicial Discretion*, 12 WILLAMETTE J. INT'L L. & DISP. RESOL. 185, 189 (2004) (noting that most transnational contracts contain a forum selection clause); William W. Park, *Text and Context in International Dispute Arbitration*, 15 B.U. INT'L L. J. 191, 192 (1997) (noting that "many international contracts include a forum selection mechanism, which typically falls into one of two categories: (i) a jurisdiction clause that grants exclusive adjudicatory competence to designated courts; or (ii) an arbitration clause that provides for disputes arising out of the contract to be settled under the rules of a relatively neutral arbitral institution"). Cf. Antonin I. Pribetic, "Strangers in a Strange Land"—*Transnational Litigation, Foreign Judgment Recognition, and Enforcement in Ontario*, 13 J. TRANSNAT'L L. & POL'Y 347, 348 (2004) ("Many [international sales] contracts include a standard clause in which the parties agree that any dispute between them is subject to arbitration or to the exclusive jurisdiction of a given court."); John Fellas, *Choice of Forum in International Litigation*, in INTERNATIONAL BUSINESS LITIGATION & ARBITRATION 2002, at 41, 69 (PLI Litig. & Admin. Practice, Course Handbook Series No. 670, 2002) ("Many contracts in the international commercial context contain forum selection clauses").

¹⁹⁷ See *Philippines*, ICSID (W. Bank) Case No. ARB/02/6 ¶¶ 174-75.

¹⁹⁸ Gaillard, *supra* note 192, at 334.

¹⁹⁹ *Philippines*, ICSID (W. Bank) Case No. ARB/02/6 ¶ 125.

²⁰⁰ *Id.* (emphasis added).

the stay would be lifted, and the Tribunal has conveniently neglected to delineate the same. Presumably, it will not lift its stay for a reconsideration of the state court's judgment on the merits (since that is tantamount to making a determination on the very obligation it has declared is reserved for the state court), but will do so where there is, for example, fraud or a "miscarriage of justice."²⁰¹ Where does one draw the line? Is there, for example, a denial of justice when the Philippines court awards an arbitrary amount not substantiated or explained in its judgment, or if the court refuses to award interest on the judgment? Even assuming such a line can be drawn, for the Tribunal to recognize only extra-contractual circumstances as justifying the lifting of the stay "means that [the] Tribunal is restricting, in practice, its jurisdiction to BIT claims only, after affirming in theory, that Article VIII and X(2) of the BIT confer on the Tribunal jurisdiction over also purely contractual claims."²⁰² It is, in other words, an exercise in inconsistency.

In carving out the particular issue of the scope of SGS's obligation as a matter governed by contract, but otherwise retaining jurisdiction over the dispute as a question for the BIT,²⁰³ the Tribunal appears to assume that the dispute has various components that may be parceled out and respectively resolved.²⁰⁴ Leaving aside the difficulties already discussed above in defining such components, the Tribunal's approach is problematic in that it distorts both the contractual forum selection clause and the relevant BIT provisions. Specifically, the settlement provisions of both the CISS Agreement and the BIT provide for the settlement of the relevant "dispute" in its entirety; the former refers "[a]ll actions concerning *disputes* in connection with the [CISS Agreement]"²⁰⁵ to the Philippines courts, and the latter authorizes the investor to refer all "*disputes* with respect to investments between a Contracting Party and an investor of the other Contracting Party."²⁰⁶ Nothing in these provisions contemplates, much less authorizes, the determination of different components of the dispute (whatever they may be) in different fora.

²⁰¹ *Crivellaro Declaration*, ICSID (W. Bank) Case No. ARB/02/6 ¶ 12.

²⁰² *Id.*

²⁰³ The Tribunal notes that a claimant may press ahead with its claim before an international tribunal where the "obstacle to admissibility" (i.e., the determination by the Philippines court in this case) has been removed. *Philippines*, ICSID (W. Bank) Case No. ARB/02/6 ¶ 171. The Tribunal also notes that "[o]ther questions could perhaps arise, even if the amount payable were to be determined by the [Philippines Courts]" *Id.* ¶ 174 n.100.

²⁰⁴ *Cf. id.* ¶ 134 (the Tribunal noting that its decision sought "to give effect to the parties' contracts while respecting the general language of BIT dispute settlement provisions").

²⁰⁵ *Id.* ¶ 137 (quoting Article 12 of the CISS Agreement) (emphasis added).

²⁰⁶ *Id.* ¶ 130 (quoting Article VIII of the BIT) (emphasis added).

2. The Tribunal's Approach in Theory

a. *The Relationship Between a Breach of Contract and a Treaty Violation Under an Umbrella Clause*

In addition to engendering substantial practical difficulties, the Tribunal's approach of staying its proceedings is theoretically misguided. At the heart of its erroneous decision is a misunderstanding of the nature of a BIT violation under an umbrella clause, and its relation to a breach of contract. Specifically, in seeking to characterize different components of the dispute as a function of a contract or a BIT, the Tribunal's approach in *SGS v. Philippines* is improperly based on that adopted in the *Vivendi* annulment decision.²⁰⁷ *Vivendi* noted that breaches of contract and breaches of treaty ultimately relate to independent standards, and that a tribunal's task in the face of a dispute that implicated both was to determine if "the fundamental basis of the claim" is the contract or the treaty.²⁰⁸ Where the claim's fundamental basis was determined to be a contract, any exclusive forum selection clause in the contract controlled the dispute; where the claim's basis was a treaty, however, the BIT's dispute settlement provisions take effect and the BIT tribunal must assume jurisdiction thereof.²⁰⁹

Significantly, however, while *Vivendi* involved an exclusive forum selection clause in the contract that referred any dispute arising there under to the courts of the host State, it did *not* involve an umbrella clause. Rather, the question was whether a BIT tribunal could dismiss claims by the investor based on alleged BIT violations that also resembled contractual claims on the ground that the intertwined "nature" of the claims made it "impossible" for the tribunal to distinguish one from the other without scrutinizing the contract, a task assigned to the state court according to the tribunal's view of the contract's forum selection clause.²¹⁰ The *ad hoc* Committee in *Vivendi* found that by "actually fail[ing] to decide whether or not the con-

²⁰⁷ *Compañía de Aguas del Aconquija, S.A. & Vivendi Universal v. Argentine Republic*, Decision on Annulment, ICSID (W. Bank) Case No. ARB/97/3 (2002), *reprinted in* 41 I.L.M. 1135 (2002).

²⁰⁸ *See Philippines*, ICSID (W. Bank) Case No. ARB/02/6 ¶ 153 (noting in support of its decision to give effect to the forum selection clause in the contract that "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") (citing *Vivendi*, ICSID (W. Bank) Case No. ARB/97/3 ¶ 98).

²⁰⁹ *See Vivendi*, ICSID (W. Bank) Case No. ARB/97/3 ¶ 101.

²¹⁰ *Compañía de Aguas del Aconquija, S.A. & Vivendi Universal v. Argentine Republic*, Award, ICSID (W. Bank) Case No. ARB/97/3, 3 (2000), *reprinted in* 40 I.L.M. 426, 428-29 (2001).

duct in question amounted to a breach of the BIT,”²¹¹ the Tribunal improperly abdicated its responsibility for making that initial determination. The forum selection clause in the contract did not relieve the Tribunal of that responsibility as:

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, such as that reflected in [the BIT provision providing for fair and equitable treatment].²¹²

In annulling the dismissal of the investors’ claims, the Committee fashioned a test for distinguishing between breaches of contract and treaty violations, which was to determine whether a claim’s “fundamental” or “essential” basis was of a contract or a treaty, and to treat it as such accordingly.²¹³

However, such an inquiry, which examines whether a claim is more akin to a contract or a treaty, is not meaningful with respect to claims based on the umbrella clause, which recognizes all contractual breaches as BIT violations, and characterizes them as such. In particular, the *Vivendi* test assumes in its distinction between the two that the relevant BIT provision sets “a distinct standard” from that contained in contracts, and does not comprehend the effects of an umbrella clause, which *defines* a BIT violation as any breach of the contract.

Significantly, while claims premised on the umbrella clause are defined by reference to the terms of contract, this act of incorporating the contract does not alter the fact that the claims ultimately *are* BIT claims whose “nature” is wholly that of treaty claims. Indeed, if it is at all applicable, the *Vivendi* test, which calls for a BIT tribunal to assume jurisdiction over claims whose “fundamental basis” is a treaty notwithstanding any exclusive forum selection clause in the contract,²¹⁴ must *a fortiori* require the same for

²¹¹ *Compañía de Aguas del Aconquija, S.A. & Vivendi Universal v. Argentine Republic*, Decision on Annulment, ICSID (W. Bank) Case No. ARB/97/3, ¶ 111 (2002), *reprinted in* 41 I.L.M. 1135 (2002).

²¹² *Id.* ¶ 105.

²¹³ *See id.* ¶ 101; *see also* *Société Générale de Surveillance S. A. v. Philippines*, Decision of the Tribunal on Objections to Jurisdiction, ICSID (W. Bank) Case No. ARB/02/6, ¶ 153 (2004), *reprinted in* 19 MEALEY’S INT’L. ARB. REP. 6 (2004).

²¹⁴ *Id.* ¶ 105. Several other cases that did not involve umbrella clauses have looked at the question of whether a BIT tribunal may exercise jurisdiction under a broad dispute resolution clause in the BIT over alleged violations of a BIT that also relate to the underlying investment contract, notwithstanding an exclusive forum selection clause in the contract. *See, e.g.,* *Salini Costruttori SpA v. Morocco*, Decision on Jurisdiction, ICSID (W. Bank) Case No. ARB/00/4 (2001), *reprinted in* 42 I.L.M. 609, 614 (2003); *LANCO Int’l, Inc. v. Argentine Republic*, Decision on Jurisdiction, ICSID (W. Bank) Case No. ARB/97/6 (1998), *reprinted in* 40 I.L.M. 457 (2001). As with *Vivendi*, these cases can be read to support a BIT tribunal exercising jurisdiction over claims based on umbrella clauses insofar as they affirm a BIT tribunal’s jurisdiction over such asserted treaty-based claims, which they do. *See, e.g., Salini*,

BIT claims as defined under the umbrella clause. Relevantly, the *ad hoc* Committee in *Vivendi* noted that “[a] state cannot rely on an exclusive jurisdiction clause in a contract to avoid the characterization of its conduct as internationally unlawful under a treaty.”²¹⁵

b. *Applicable Principles of Contractual Interpretation*

Not only is the basis of the Tribunal’s decision to stay the proceedings suspect, the Tribunal’s interpretation and application of particular principles of contract law to resolve the conflict between the BIT and the contract is likewise mistaken.

The Tribunal declined to read BIT provisions as overriding forum selection clauses in contractual claims on the ground that a general provision in a broad framework treaty should not be presumed to take precedence over a specific provision in a negotiated contract.²¹⁶ In particular, the Tribunal considered such an interpretation implausible, as it would otherwise be impossible to hold investors to any agreement to an exclusive jurisdiction clause in their contracts since “they will always have the hidden capacity to bring contractual claims to BIT arbitration.”²¹⁷

But this premise is false. It is entirely open to States to introduce language in their BITs limiting the effect umbrella clauses and/or BIT settlement provisions have on contracts containing a forum selection clause.²¹⁸ Alternatively, with respect to investment contracts existing at the time of the BIT, a State could have inserted language in the BIT specifically excluding any such contract from its scope. Similarly, in the case of investment contracts entered into after the BIT was concluded, the State could have inserted language in those contracts excluding the application of any

ICSID (W. Bank) Case No. ARB/00/4 ¶¶ 61, 62 (determining *inter alia* that the BIT tribunal has jurisdiction to hear all claims based on a violation of the BIT and over contract breaches that simultaneously amounted to BIT violations notwithstanding a contractual forum selection clause).

²¹⁵ *Compañía de Aguas del Aconquija, S.A. & Vivendi Universal v. Argentine Republic*, Decision on Annulment, ICSID (W. Bank) Case No. ARB/97/3, ¶ 105 (2002), *reprinted in* 41 I.L.M. 1135 (2002).

²¹⁶ *Société Général de Surveillance S. A. v. Philippines*, Decision of the Tribunal on Objections to Jurisdiction, ICSID (W. Bank) Case No. ARB/02/6, ¶ 141 (2004), *reprinted in* 19 MEALEY’S INT’L. ARB. REP. 6 (2004).

²¹⁷ *Id.* ¶ 134.

²¹⁸ *See Société Général de Surveillance S. A. v. Philippines*, Decision by One of the Arbitrators (“Crivellaro Declaration”), ICSID (W. Bank) Case No. ARB/02/6, ¶ 5 (2004), *available at* <http://www.worldbank.org/icsid/cases/SGSvPhil-declaration.pdf> (noting that “A BIT can certainly limit the investor’s freedom of choice, for instance providing that a forum which has already been agreed in a past investment agreement remains the “exclusive” forum for disputes arising from that investment agreement. Such a limitation is not uncommon in BITs practice”).

relevant BIT to such contracts (and can continue to do the same for future contracts). The latter possibility explains why simply applying a *presumption* that BIT provisions override the forum selection clause in general does not mean, as the Tribunal contends, that a “government [has agreed] to the adjudication for the future of an indefinite range of cases in a number of different forums with different rules.”²¹⁹

Rather, the proper question here is whether the onus should be on the State or the investor to clarify any potential conflict between the BIT and the contract. Significantly, as between the State and investor, the State alone is party to both agreements. Accordingly, only the State can be held responsible for such conflict, and any resulting ambiguity must be construed against it and in favor of the investor. Thus, in *SGS v. Philippines*, since the Philippines alone was party to both the BIT and the CISS Agreement (with SGS being party only to the latter), the conflict between the BIT provisions and Article 12 of the CISS Agreement should be resolved against the Philippines.

The Tribunal also relies on the principle that “a party to a contract cannot claim on that contract without itself complying with it.”²²⁰ But this ignores the umbrella clause’s effect, which, as explained above, makes it a violation of the *BIT* to breach the contract. That the umbrella clause incorporates the terms of the contract in defining a BIT violation does not change the singular treaty character of the resulting BIT violation.

Additionally, the party here, SGS, based its claim on the BIT. As the Tribunal itself acknowledged, “it is for the Claimant to formulate its case. Provided the facts as alleged by the Claimant and as appearing from the initial pleadings fairly raise questions of breach of one or more of the provisions of the BIT, the Tribunal has jurisdiction to determine the claim.”²²¹

Taken together, the reference point for the inquiry is the BIT and not the contract. It could equally be said of the Philippines that *it* should not be entitled to reap the benefits of the BIT (for example, in encouraging continued investment) without being bound by its obligations. Since the issue here concerns a BIT violation and not a mere contractual breach, it is the State that “should not be able to approbate and reprobate in respect of the same agreement.”²²² Accordingly, SGS should be entitled under the BIT provisions to bring claims based on breaches of contract to the Tribunal.

²¹⁹ *Id.* ¶ 153. For the same reason, the dissent’s suggestion that the umbrella clause should apply only to contracts concluded before the BITs where the BIT does not clarify any potential conflict between the two is mistaken. *See supra* Part IV.B.2.a.

²²⁰ *Philippines*, ICSID (W. Bank) Case No. ARB/02/6 ¶ 154.

²²¹ *Id.* ¶ 157.

²²² *Id.* ¶ 155.

C. *The Broader Sanctity of Contract Principle*

In interpreting the umbrella clause, the Tribunal's overarching task is to determine what the Contracting States agreed would be the effect of the clause. To do so in accordance with well-established principles of international law, the Tribunal needs to read the clause objectively to determine its meaning.²²³ As discussed above, the most reasonable interpretation of a broadly worded clause in light of its plain language, history and purpose is that it applies without exception to investment contracts.²²⁴ This, then, is what we must deem the parties to have agreed upon. Having made this bargain, it is imperative that the Contracting States be held to their agreement.

Critically, at stake here is the investor's ability to resolve contractual investment disputes in a neutral and international forum, a core benefit of the BIT affirmatively provided for under the agreement between the Contracting States, and, therefore, one the investor legitimately expects to receive. Allowing the host State to renege on its agreement creates uncertainty in the global marketplace and can serve only to discourage foreign investment, a result at odds with the very purpose of BITs. The more broadly applicable principle here, therefore, is that of the sanctity of contract, not simply as between the host State and the investor over an investment contract, but also as between Contracting States over a BIT.

D. *A Summing Up of the Umbrella Clause's Proper Construction*

The Tribunal's decision in *SGS v. Philippines* to stay its proceedings is erroneous. Not only is the rationale based on a misapprehension of the nature of a BIT violation as defined under an umbrella clause and the applicable rules for resolving conflicts between BITs and investor-State contracts, it has the practical consequence of eviscerating the umbrella clause itself. An exclusive contractual forum selection clause should not be permitted to prevail over the umbrella clause and the BIT's dispute settlement provisions. There are two reasons the forum selection clause should not prevail. First, a BIT violation arising under the umbrella clause is no less redressible under the BIT for being defined by reference to the contract (whose terms are simply incorporated into the umbrella clause). Second, the conflict between BIT provisions and the forum selection clause in the contract arises from an ambiguity that should be resolved against the State, who alone is party to both the BIT and the contract.

²²³ See *supra* text accompanying notes 177-80.

²²⁴ See *supra* Part IV.A-B.

Thus, to answer the two-part question posed by this article on umbrella clauses, the more reasonable and effective interpretation of the umbrella clause is that it applies to obligations arising under the relevant investor-State investment contract, and a BIT tribunal may thereby exercise jurisdiction over breach of contract claims, including when the contract contains an exclusive forum selection clause.

V. A BROADER PERSPECTIVE ON THE UMBRELLA CLAUSE DEBATE

On one level, the problem of the umbrella clause is about what principles of contractual interpretation should be brought to bear on a provision that redefines the relationship between contractual breaches and treaty violations in investor-State disputes. But there is a broader perspective that takes into account the history and nature of investment arbitration. Namely, that it manifests the long-standing tension between the priorities of developing as opposed to developed nations in the context of foreign investment.

A. *The Asymmetrical Effect of Umbrella Clauses*

Historically, foreign investment capital flowed principally in one direction—from developed to developing countries.²²⁵ As such, a significant proportion of BITs are between a developed country on the one hand and a developing country on the other.²²⁶ Therefore, even though the BIT imposes

²²⁵ See Catherine Brown & Christine Manolakas, *Trade in Technology Within the Free Trade Zone: The Impact of the WTO Agreement, NAFTA, and Tax Treaties on the NAFTA Signatories*, 21 NW. J. INT'L L. & BUS. 71, 97 n.176 (2000) (noting that "capital investment flows primarily from the developed country to the developing country").

²²⁶ Teresa McGhie, *Bilateral and Multilateral Investment Treaties*, in LEGAL ASPECTS OF FOREIGN DIRECT INVESTMENT 107, 108 (Daniel D. Bradlow & Alfred Escher, eds., 1999) ("Most BITs are between a developed or capital exporting country and a developing country."). Also, the WORLD INVESTMENT REPORT, *supra* note 5 at 27, notes that as of the end of 2004, forty percent of BITs concluded were those between developed and developing countries. Critically, the WORLD INVESTMENT REPORT does not simply divide the world into developing and developed countries, but also includes two other categories, namely South East Europe and the Commonwealth of Independent States, which includes all of the republics that were part of the former USSR, except the Baltic States. See WORLD INVESTMENT REPORT, *supra* note 5, at 6, 27. Additionally, the eight of the ten countries that joined the European Union on May 1, 2004 (and that were formerly classified as part of Central and Eastern Europe) were reclassified as developed countries. *Id.* Assuming one classifies these countries as either "developed" or developing," and depending on how one does this, the percentage of BITs concluded between developed and developing countries may well be much higher. *Cf. id.*

Note, however, that in recent years, an increasing percentage of BITs are concluded between developing countries. Indeed, the "largest number of the new BITs signed during 2004 was between developing

reciprocal obligations on both Contracting States, its effects are asymmetrical since the host State is typically a developing country while the investor is often a national from a developed country. The result is that developing countries will seek to interpret restrictively any BIT provision that accords rights to the investor and imposes obligations on the Host state favoring investors, whereas developed countries will read the same provision expansively. The umbrella clause is a prime example of such a BIT provision, as evidenced by the fact that the disputes in both *SGS* arbitration proceedings have played out along these same lines: with Pakistan and the Philippines (the developing countries) calling for a restrictive interpretation of the umbrella clause, and investors from Switzerland (the developed country) seeking a broader interpretation.²²⁷

This divide separating developed and developing countries in foreign investment disputes dates back to the formative years of international investment law itself. As described earlier in this article,²²⁸ there was no coherent legal regime relating to foreign investments in the first half of the twentieth century. What international legal principles existed concerning investment rights and obligations were often vague and open to wide-ranging interpretation. While industrialized countries asserted that international law imposed various obligations on host states to protect foreign investments and to compensate for their expropriation, newly decolonized and developing countries decried such a view as serving only to entrench industrialized nations' economic dominance and to curb their ability to manage resources within their own borders, thereby infringing on their sovereignty.²²⁹

countries, with 28 BITs or 38% of the total, followed closely by BITs between developed and developing countries with 27 of all BITs signed." *Id.* at 24. As such, the perspective discussed in this article that the conflict over the interpretation of BIT provisions is one between developed and developing countries will begin increasingly to lose its currency. Nonetheless, as matters stand and certainly from a historical viewpoint, this perspective remains valid.

²²⁷ Notably, it is not merely the investors but also their governments who advocate an expansive interpretation of the umbrella clauses. This is hardly surprising since governments would be expected to champion the causes of their nationals. Case in point: After the *SGS v. Pakistan* decision was rendered, the Swiss authorities sent a letter to the ICSID Secretariat noting that they were "alarmed about the very narrow interpretation given to the meaning of [the umbrella clauses of the Switzerland-Pakistan BIT], which . . . runs counter to the intention of Switzerland . . ." Note on the Interpretation of Article 11 of the Bilateral Investment Treaty between Switzerland and Pakistan in the light of the Decision of the Tribunal on Objections to Jurisdiction of ICSID in Case No. ARB/01/13 *SGS Société Générale S.A. versus Islamic Republic of Pakistan*, attachment to Letter from Marino Baldi, Swiss Secretariat for Economic Affairs, to the ICSID Deputy-Secretary General (Oct. 1, 2003), *reprinted in* 19 *MEALEY'S INT'L ARB. REP.* 1 (2004).

²²⁸ See Introduction *supra*.

²²⁹ See *id.*

As the dispute over the construction of the umbrella clause shows, this conflict between the two sides persists to the present day, even if the talking points of the debate have evolved. While the earlier disagreement was over what standards applied to the treatment of investments under international law, the current dispute is over how agreed-to standards of treating investments should be interpreted.

B. *First World vs. Third World: The Question of Unconscionable Contracts*

Under this broader perspective, the debate over umbrella clauses is not simply a conflict between investors and host States, but one between developed and developing countries. Accordingly, one might argue that in favoring investors over host States, the broader interpretation of umbrella clauses advanced here also favors developed countries over developing nations, and such a result may be inequitable because of the presumably greater bargaining power that developed countries have over their developing counterparts. In other words, to enforce the umbrella clause is possibly to enforce an unconscionable contract against a developing country under economic pressure to enter into a BIT containing such a clause. This argument is flawed, however.

For one thing, one may equally contend that an investment contract that exclusively refers disputes to a local forum is in fact an unconscionable contract favoring the host State and, therefore, developing countries. The leverage that a host State has in any particular contract may be greater than the investor since it is dealing with individual companies that presumably face competition in the global marketplace. It is difficult, for example, to see how SGS could have been content to submit its disputes to the Philippines courts rather than international arbitration if the playing field were entirely level.

Relevantly, it bears observing that the enforcement of umbrella clauses does not lead to a final award on the merits in favor of the investor; it results rather in an arbitral procedure for resolving the dispute that does not inherently favor either party.²³⁰ Both parties will have equal say in the appointment of the tribunal, which will only then begin to consider the merits of the dispute.²³¹ Contrast this with the enforcement of an exclusive forum selection clause like the one in *SGS v. Philippines*, where a state court has to resolve a case involving the state government as one of the interested

²³⁰ See generally REED ET AL., *supra* note 3, at ch. 4 (on ICSID arbitration procedure, including with respect to the constitution of the tribunal).

²³¹ *Id.*

parties. This latter scenario surely poses the greater risk that one of the parties, in this case, the investor, will not receive a fair hearing. Thus, all else being equal, it is arguably better to err on the side of the umbrella clause prevailing over the exclusive forum selection clause insofar as it insures a more equitable result, or at least is seen to do so.

More generally, it should be noted that while the effect of adopting the interpretation proposed favors investors and developing countries, that result did not serve as its *motivation*. Rather, this reading of the umbrella clause was arrived at through applying the objective, methodical process of interpreting the BIT, relying both on the relevant language and history of the clause according to well-established principles of international law.²³² That the interpretation happens to favor either party simply follows from the assessment of what the parties can be said objectively to have agreed upon.

CONCLUSION

Under this broader perspective, the question of the proper interpretation of umbrella clauses is but the latest chapter in the long-running saga of conflict between the foreign investment interests of developing and developed countries. Even so, this particular chapter is unnecessarily controversial, and more significantly, threatens unjustifiably to close the book on umbrella clauses. How ironic to find that a clause aimed at preserving the sanctity of contract is itself at risk of being written off by a larger failure to respect agreements—not just contracts as between a state and an investor, but also treaties as between states themselves. Here's hoping there's a coda to this story where its hero comes back to life and gets the happy ending it deserves.

²³² See discussion *supra* Part III.