Is the Umbrella Clause Not Just Another Treaty Clause?

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The issue of the validity of the umbrella clause as a basis of claims requires more detailed analysis in light of the divisions that are apparent in the awards.

M. Sornarajah

Introduction

Today, the ‘umbrella clause’ continues to divide legal opinion. Its basis and effects remain unsettled. The clause is often said to ‘internationalise’ state contracts by rendering them effective under international law. This chapter challenges the idea of internationalisation.

Much of the controversy surrounding umbrella clauses has had to do with the idea of the internationalisation of contractual commitments. Professor Sornarajah called the idea of internationalisation a ‘myth’, not least because the argument has tended to rely upon the ‘low-order sources’ of international law as the basis for claiming the sanctity of contracts under international law. However, umbrella clauses, too-long

4 Sornarajah, International Law on Foreign Investment, 3rd ed., 304. Sornarajah also links the intended effects of umbrella clauses to those of stabilisation clauses, Id.
ignored, have always had a sound basis in treaty law. These clauses do not have to rely upon the low-order sources of international, but the straightforward application of the doctrine *pacta sunt servanda* between states.

This chapter argues against the widespread idea that the underlying contract is itself, necessarily, ‘elevated’ by the umbrella clause to the international plane. Instead, such a treaty clause simply purports to treat breaches of certain contractual and other undertakings as straightforward treaty violations. Viewed in this way, umbrella clauses should be treated like any other garden-variety treaty clause, requiring only the ordinary methods of treaty interpretation to be applied to their construction.

This is one way of approaching criticism of the supposedly ‘automatic, sweeping and unqualified’ effect of umbrella clauses, in the words of the *SGS v. Pakistan* tribunal; precisely because the umbrella clause in that Award was argued to have had the supposed effect of elevating the underlying contract itself to the international plane. Similar objections by critics of the umbrella clause have, in practice, lent support to a restrictive reading of umbrella clauses. It is thought that the notion that we can turn every contractual commitment into an equivalent treaty commitment would allow private parties to ‘expand’ the content of the treaty commitments undertaken by the host state. As such, in *SGS v. Pakistan*, the tribunal required ‘clear and compelling’ evidence for saying that such an elevation had originally been intended by the treaty parties.

Today, opposed to *SGS v. Pakistan* and its progeny is a separate line of authorities constituted by the Awards in cases such as *SGS v. Philippines*, and *Noble Ventures v. Romania*. These Awards would require only the interpretation of the plain words of the treaty. No theory of internationalisation is involved.

However, more recent cases which have taken the kinds of concern expressed in *SGS v. Pakistan* seriously have sought to rely on some form of decisive contractual, private law or other factor in seeking to limit or deny the application of umbrella clauses. They include the idea that much

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6 *SGS v. Pakistan*, ICSID Case No. ARB/01/13, Decision on Objections to Jurisdiction, 6 August 2003.
7 It could be argued in response that this was precisely what the contracting states envisaged, and had intended.
8 *SGS v. Philippines*, ICSID Case No. ARB/02/6, Decision on Jurisdiction, 29 January 2004.
9 *Noble Ventures v. Romania*, ICSID Case No. ARB/01/11, Award, 12 October 2005.
could depend upon whether the state’s contractually violative acts took the guise of *acta jure imperii*, giving voice to the neglected role of contractual forum selection clauses and to the doctrine of privity of contract. There is also the suggestion that fair and equitable treatment (FET) clauses already operate as ‘de facto umbrella clauses’, or even that umbrella clauses ought to be rendered effective only in tandem with other treaty standards.

The origin and definition of the umbrella clause

*Origins and rationale*

An early and influential illustration of an umbrella clause may be found in the Abs/Shawcross Draft Convention, a privately sponsored joint-initiative by the former Deutsche Bank chairman, Hermann Abs, and Sir Hartley (later Lord) Shawcross.

Historically, the notion of the international sanctity of contracts might be viewed in light of the attempt by the United States to promote that idea, in tandem with that of international arbitration, before the United Nations General Assembly in the early 1960s. That attempt was a prelude to the modern bilateral investment treaty (BIT) movement, which, at the same time, had incorporated umbrella clauses early on. Umbrella clauses were also part of a two-fold project – not only to secure recognition of the international sanctity of private contracts but also to subject investment contract disputes to binding international arbitration. The reason treaty law ultimately became the preferred source of

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international law for securing the international sanctity of private contracts was precisely because other alternative bases for internationally enforcing contractual commitments had been controversial.\textsuperscript{14}

Definition

An umbrella clause may be defined broadly. It is a treaty clause which extends the scope of the independent protection of the treaty to breaches of contractual and other domestic commitments relating to the foreign investor’s investment.

Sceptics might ask why, when there is such widespread substantive treaty protection today, umbrella clauses might be thought to perform any function at all without making these other treaty forms of protection redundant. One answer is that the umbrella clause does not simply provide parallel protection in tandem with other treaty rights. Rather, it expands the scope of the treaty protection by including contractual commitments which do not always fall within the FET, full protection and security and expropriation clauses. That is the gravamen of the matter. Umbrella clauses are controversial precisely because they are not superfluous.

But are they as expansive as the tribunal in SGS v. Pakistan suggested? To use a well-worn example from trade law regulation, it might be thought that in their construction such clauses are akin to an accordion\textsuperscript{15} and may be stretched widely or squeezed narrowly. That recent attempts have been made to revisit the language of these clauses only reinforces the point by showing that there is a wide variety of such clauses today.\textsuperscript{16} However, one line of authorities – following SGS v. Pakistan – has insisted that, if permitted, umbrella clauses would effectively allow private parties to negotiate and infinitely expand the scope of protection given under a treaty deal struck between two or more sovereign

\textsuperscript{14} SGS v. Pakistan, ICSID Case No. ARB/01/13, Decision on Objections to Jurisdiction, 6 August 2003, footnote 108 at para. 98, citing the Claimant’s argument which had relied upon R. Dolzer and M. Stevens, \textit{Bilateral Investment Treaties} (Hague: Nijhoff, 1995), 81–82, a comment expressed by the late Ibrahim Shihata and Professor Christoph Schreuer’s opinion.

\textsuperscript{15} Trade lawyers know this analogy, see \textit{Japan – Alcohol}, WT/DS8/AB/R, 1 November 1996.

\textsuperscript{16} See the definition of “investment agreement” as defined in Article 1 of the 2012 US Model BIT, which is also discussed in Chapter 9. That definition curtails the operation of the current version of a US umbrella clause contained in Article 24 of the 2012 Model BIT. \textit{Contra} the earlier example of such a clause in Article II(2)(c) of the US–Argentina BIT.
contracting parties. In a similar vein, Sornarajah has argued that such clauses are in effect ‘catch-all statements’.17

Sornarajah’s scepticism

As we have seen, umbrella clauses purport to achieve what theories about the internationalisation of contracts have long sought – the international sanctity of private law contracts. The tribunal in *SGS v. Philippines* acknowledged this,18 although – unlike the tribunal in *SGS v. Pakistan* – it refused to decide whether an umbrella clause would necessarily elevate or internationalise every contractual breach. As we shall see, the notion of internationalisation also became a point of criticism in the subsequent Award in *Noble Ventures v. Romania*.19

Sornarajah, who had begun his career by writing on investment contracts, has been a long-standing, well-known critic of the notion of internationalised state contracts.20 He explains two broad historical versions of the idea. The first had to do with the importance, from the viewpoint of investors, of effecting some choice or selection of international or at least neutral, non-national law to govern contracts between host states and foreign investors.21 The second and more ‘extreme’ theory, often associated with the view of the arbitrator in *Texaco v. Libya*,22 does away altogether with the need for party choice and asserts that objectively viewed contracts can become ‘internationalised’ where

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17 The phrase appears in Sornarajah’s *International Law on Foreign Investment*, 3rd ed., 215 (in which the term “umbrella clause” is also used). For the second edition, see *The International Law on Foreign Investment*, 2nd ed. (Cambridge: CUP, 2004), 248.
19 *Noble Ventures v. Romania*, ICSID Case No. ARB/01/11, Award, 12 October 2005.
21 Sornarajah, *International Law on Foreign Investment*, 3rd ed., 289 (“The removal of the foreign investment transaction from the sphere of the host state’s law and its subjection to an immutable system is seen as essential for the protection of foreign investment under the theory of internationalisation.”) See also his treatment of this point in Sornarajah, “Myth”, 187, 202.
the intent of the parties may be shown through arbitration and stabilisation clauses too in long-term, high value contracts.\textsuperscript{23}

Sornarajah has dismissed the whole idea as a myth\textsuperscript{24} and wrote of that seemingly ‘mystical quality’ which, it is alleged, somehow enables state contracts ‘to levitate’.\textsuperscript{25} Sornarajah argues that contracts are valid by virtue of some domestic legal system, not by virtue of international law. There are treaty rights, rights under customary international law, and then there are private law contractual rights. But there is no such beast as an ‘international contractual’ right in the fauna of municipal and international rights.

His is no semantic quibble. It has been the conventional view. The \textit{Serbian Loans} case had long been standard authority,\textsuperscript{26} in which the Permanent Court of International Justice had considered contracts to be mere creatures of municipal, not international, law. Lord Radcliffe had held a similar view in the English case of \textit{Kahler v. Midland Bank}.\textsuperscript{27}

Umbrella clauses are, however, different. They at least observe the confines of conventional international legal doctrine. The question which such clauses pose is not whether the underlying contracts are in the end analysis only creatures of municipal law or whether they might have become ‘international’ contracts, but rather, whether the breach of the underlying contract ought in certain circumstances to be considered a treaty violation as a matter involving the ordinary construction of a treaty clause. Recall that a decade ago in \textit{Noble Ventures v. Romania}, the

\textsuperscript{23} Sornarajah, \textit{International Law on Foreign Investment}, 3rd ed., 294 (“The more extreme variety of the theory of internationalisation is that the very nature of the foreign investment contract gives rise to the inference that it is subject to a supranational system of law.”)

\textsuperscript{24} Sornarajah, “Myth”, \textit{op. cit.} Sornarajah has been especially critical of F.A. Mann’s view of the existence of a “commercial law of nations”, based in part upon Mann’s reading of one of the well-known arbitral Awards from the 1950s – the \textit{Abu Dhabi Arbitration} (1951) 19 ILR 144 – for which Lord Asquith is commonly cited in favour of the existence of such a body of laws; F.A. Mann, \textit{Studies in International Law} (Oxford: OUP, 1972), 143; \textit{contra} Sornarajah, “Myth”, 199, 201, 202. Where Mann criticised the defenders of the developing country viewpoint for being subjective, Sornarajah countered by criticising Mann and others for their thinly disguised efforts to serve the interests of Western capital; F.A. Mann, “Wrong in National and International Law”, (1977) 48 BYbIL 1; \textit{contra} Sornarajah, “Myth”, 199.

\textsuperscript{25} That is, out of the sphere of domestic law into that of international law; M. Sornarajah, \textit{Law of International Joint Ventures} (Spore: Longman, 1992), 298.

\textsuperscript{26} PCIJ No. 14, Ser. A, No. 20 at 41 (“Any contract which is not a contract between states in their capacity as subjects of international law is based on the municipal law of some country.”)

\textsuperscript{27} [1950] AC 24, 56 \textit{per} Lord Radcliffe.
tribunal there had considered that a contractual breach has of itself nothing to do with international law unless it also amounts to a violation of a treaty standard. That Award is now cited for its support of umbrella clauses, but its chief value lies in the important distinction drawn between questions about the source of contractual validity and international treaty clauses which purport to govern the consequences of contractual breach.

Similarly, a controversy arose when the Vivendi tribunal upheld a contractual stipulation which required the dispute to be resolved locally before the Tucuman administrative courts. That tribunal had found the rights in question under the French–Argentine BIT to have been ‘inseparable’ from the contractual rights under a 30-year provincial concession contract. The Annulment Committee,28 however, considered treaty and contractual rights to be separate and distinct. Thus, for the Annulment Committee, the contractual choice of the Tucuman courts did not mean that Vivendi’s treaty rights could then be ignored or extinguished.29 Each source of law – contract and treaty – existed within its own proper sphere.

Likewise, the Annulment Committee in CMS v. Argentina had emphasised that ‘The effect of the umbrella clause is not to transform the obligation which is relied upon into something else; the content of the obligation is unaffected, as is its proper law’.30

The source of contractual validity remains the applicable law of the contract. The contract continues to be governed by that law in respect of the usual incidents of contract notwithstanding any treaty consequences which may apply to its breach.31

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28 Compañía de Aguas del Aconquija SA and Vivendi Universal v. Argentina, ICSID Case No. ARB/97/3, Decision on Annulment, 3 July 2002 (hereafter, Vivendi, Annulment).
29 Id., para. 96.
30 ICSID Case No. ARB/01/8, Decision on Annulment, 25 September 2007, para. 95(c).
31 In addition to Serbian Loans, PCIJ No. 14, Ser. A, No. 20 at 41 and Kahler v. Midland Bank [1950] AC 24, 56, this view also has the benefit of distinguished support in the sphere of academic commentary. H. Lauterpacht, Private Law Sources and Analogies of International Law (London: Longman, 1927), 156. Writers who compare treaties to contracts merely draw an analogy, and indeed the proposition was that treaties between states are “as binding” under international law as contracts between individuals under municipal law, see e.g. B. Cheng, General Principles of Law as Applied by International Courts and Tribunals” (London: Stevens, 1953), 112 (on the doctrine of pacta sunt servanda). Successive editions of Brownlie treated the Serbian Loans case under the rubric of “Issues of Municipal Law before International Tribunals”, notwithstanding the fact that the contract in that case was between French bondholders and the Serb-Croat-Slovene Government. Brownlie never wavered from the view that: “The rules of public international law accept the normal
Observing the language of the umbrella clause

Let us then assume that umbrella clauses do not, or at least do not necessarily, presuppose any theory of internationalisation, elevation, transformation or similar notion. The treaty clause would presuppose the need for strict contractual analysis – of the validity of the contract, its terms, and breach – but what kinds of treaty clauses would be required to create such hybrid treaty rights?

The Abs/Shawcross formula and its progeny

As an example, the clause in the 1990 UK–Argentina BIT states:32

Each Contracting Party shall observe any obligations it may have entered into with regard to the investments of investors of the other party.

This resembles the clause in the Abs/Shawcross Draft Convention on Investments Abroad today,33 as opposed, for example, to the clause in operation of rules of private international law and when a claim for a breach of contract between an alien and a government arises, the issue will be decided according to the applicable system of municipal law designated by the rules of private international law”. This was what Serbian Loans had been about. The position would be no different even if the contractual parties were to choose public international law as the applicable law. In practice, international law would be chosen alongside municipal law where “in the face of such clauses arbitrators have a certain discretion in selecting the precise role of public international law.”

But, the view that the contractual selection of public international law as the applicable law places the contract on the international plane “cannot be correct”. See I. Brownlie, Principles of Public International Law, 7th ed. (Oxford: OUP, 2008), 37, 549–550. Though seemingly plausible since a sovereign intention to be bound by law transpires, the argument that this makes that binding law international law has been criticised by Sornarajah as a political invention born of the fears of the “European club of States” during the post-colonial era. See M. Sornarajah, International Commercial Arbitration: The Problem of State Contracts (Spore: Longman, 1990), 123. To be sure, internationalisation had been advanced by equally distinguished commentators, counting McNair, Verdross, Mann and von Mehren among them; A. McNair, “The General Principles of Law Recognised by Civilised Nations”, (1957) 33 BYIL 1; I. Seidl-Hohenveldern, “Recollections of Alfred Verdross”, (1994) 5 EJIL 98, 102; Mann, Studies, 143; A. von Mehren, “Special Substantive Rules for Multistate Problems”, (1974) 88 Harv. L. Rev. 347. Sornarajah’s response was that if there had ever been cause for gap-filling by such low-order sources of law as the general principles of law recognised by civilised nations, or the general principles of law, this lasted for only so long as there were no comprehensive national rules on the part of developing nations on foreign direct investment; Sornarajah, Joint Ventures, 299.

33 Art. 2, Draft Convention on Investments Abroad, 1959, Article II; reproduced in Newcombe and Paradell, Law and Practice of Investment Treaties, 441, states that: “Each Contracting Party shall at all times ensure the observance of any undertakings, which it may have given in relation to investment made by nationals of any other party”.
Article 2(4) of the Italy–Jordan BIT in Salini v. Jordan, which is worded entirely differently:\(^{34}\)

Each Contracting Party shall create and maintain in its territory a legal framework apt to guarantee to investors the continuity of treatment, including the compliance, in good faith, of all obligations assumed with regard to each specific investor.

Observe, in particular, the phrase ‘any obligations’ in the above-mentioned British–Argentine example. That lends itself to an expansive reading, but it is then qualified by the phrase ‘it may have entered into’, suggesting that the clause applies only to specific undertakings. Compare that with the absence of any stipulation at all in the Italian–Jordanian example about the observance of commitments. As the International Centre for the Settlement of Investment Disputes (ICSID) tribunal in Salini went on to explain, Italy and Jordan had failed to commit themselves in plain terms to the observance of ‘any obligation’ in respect of investments, let alone the ‘specific’ investments of investors of the other party.\(^{35}\)

Thus, one starts with the treaty clause itself.

The two ‘SGS’ cases

Salini had been decided after two well-known cases – SGS v. Pakistan and SGS v. Philippines. Most discussions of the subject of umbrella clauses today begin by recalling how the SGS v. Pakistan tribunal had rejected the purported umbrella clause in the Switzerland–Pakistan BIT, while the SGS v. Philippines tribunal subsequently upheld the umbrella clause in the Switzerland–Philippines BIT. This rendition places too much emphasis on outcome alone.

Article 11 of the Switzerland–Pakistan BIT in SGS v. Pakistan had been drafted in the following way. It begins, with my emphasis, by stating that ‘Either Contracting Party shall constantly guarantee the observance of the commitments it has entered into’. Notice the absence of the more expansive Abs/Shawcross phrase ‘any undertakings’. The tribunal in SGS

The use of the word “any” before the word “obligations” in the UK–Argentine BIT earlier, and before the word “undertakings” in the Abs/Shawcross version, is considered significant today; see Noble Ventures v. Romania, discussed further below, para. 62.

\(^{34}\) ICSID Case No. ARB/02/13, Decision on Jurisdiction, 9 November 2004.

\(^{35}\) Discussed also in Noble Ventures v. Romania, ICSID Case No. ARB/01/11, Award, 12 October 2005, para. 49.
v. Pakistan emphasised, in what is now a famous statement, that the underlying contractual claims were not to be assumed to have automatically been 'elevated' to the level of a treaty claim. This must be correct, since the violation of a commitment to constantly guarantee the observance of commitments is not the same thing as the violation of the guarantee itself.

The tribunal’s use of the metaphor that the contractual commitment might have become ‘elevated’ goes to the heart of the issue. It had seemingly originated in counsel’s (Monsieur Gaillard’s) submission that:

... I myself prefer to call it a mirror effect clause, because in fact it is a mirror effect which it creates.

You have a violation of the contract, and the Treaty says, as if you had a mirror, that this violation will also be susceptible to being characterised as a violation of the Treaty. So the same facts, the same breach will be a violation of the contract in itself, and a violation of the Treaty.

And that:

If I am the government and if I breach a contract, by the same token I will breach a treaty, so the useful effect of this is to create this mirror effect, to say that I will elevate in essence, and that’s what it does, it may be far-reaching but that’s what it does, to elevate breaches of contract as breaches of a treaty.

As it turned out, learned counsel had risked putting the argument at its highest.

Voss, who has devoted discussion to the matter, shows how all this might have occurred. Admittedly, the ‘elevation’ theory has had a long pedigree in the scholarly literature; beginning with Prosper Weil’s 1969 Hague Academy Lectures, where Professor Weil then spoke of an ‘umbrella treaty’ between the host and home state ‘which turns the obligation to perform the contract into an international obligation of the contracting state’ and which ‘transforms contractual obligations into international obligations’. Monsieur Gaillard had himself written about

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36 SGS v. Pakistan, ICSID Case No. ARB/01/13, Decision on Objections to Jurisdiction, 6 August 2003, paras. 166–173; also discussed by the tribunal in Noble Ventures, ICSID Case No. ARB/01/11, Award, 12 October 2005, para. 47.
37 Id., para. 99. 38 Id.
a ‘mirror effect’ of the contractual commitments in the treaty realm. But while these metaphors – of elevation, transformation or a mirror effect between the two worlds of contract and treaty – have exercised a painful hold on our imagination, in SGS v. Pakistan it was an especially generous way of reading the words ‘shall constantly guarantee the observance of the commitments it has entered into’.

In contrast, the Switzerland–Philippines BIT’s umbrella clause in SGS v. Philippines had stated – again with added emphasis – as follows:

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.

The tribunal in SGS v. Philippines duly observed that the word ‘shall’ suggested the existence of a legal obligation, and that the phrase ‘any obligation’ (which is similar to the Abs/Shawcross phrase ‘any undertakings’ and which was missing from the Swiss–Pakistani BIT) included future obligations which the host state will assume. It considered that the principle of effectiveness in treaty interpretation requires effect to be given to the clause within the framework of a treaty whose object and purpose was to be ‘the promotion and reciprocal protection of investments.’ It was perfectly consistent with the BIT therefore that contractual commitments which were intended to be binding under their own applicable law should also have been brought within the scope of the BIT umbrella clause’s protection, and that disputes concerning the scope and application of that protective umbrella will be subsumed within the investor-state arbitration clause in the BIT.

However, as I shall go on to discuss further, the SGS v. Philippines tribunal refused to adopt the theoretical view urged by Monsieur Gaillard in SGS v. Pakistan earlier. While the outcomes in the two cases were opposed, it is not without irony that the tribunal in SGS v. Pakistan had ended up assuming the more expansive view of the basis and effects of umbrella clauses even if it did not support the existence of an umbrella clause in the Swiss–Pakistani BIT.


41 SGS v. Philippines, ICSID Case No. ARB/02/6, Decision on Jurisdiction, 29 January 2004, paras. 115–116, 127; discussed in Noble Ventures, ICSID Case No. ARB/01/11, Award, 12 October 2005, para. 48 and Eureko BV v. Republic of Poland, Ad Hoc Arbitration, 19 August 2005 (Partial Award), para. 255.
Noble Ventures v. Romania

Then came the tribunal in Noble Ventures v. Romania whose attention having been directed to the two SGS cases considered that the clause in that dispute should be construed according to its plain meaning. Art. II (2)(c) of the US–Romania BIT of 1994 had stated, again I add emphasis, as follows:

Each Party shall observe any obligation it may have entered into with regard to investments.

The tribunal applied Art. 31 of the Vienna Convention on the Law of Treaties looked to the ordinary meaning of the treaty language in light of the treaty’s object and purpose and proceeded to interpret those terms in good faith. Supplementary materials may be consulted, said the tribunal, in order to confirm the meaning arrived at as a result of an interpretation of the ordinary meaning of the treaty clause. The principle of effectiveness – once described eloquently as that principle which would make treaty terms ‘a means of fulfillment rather than an exercise in futility’ – should also be observed.

Proceeding in the manner described, the tribunal considered, first, that the word ‘shall’ denotes the existence of a treaty obligation. Secondly, it considered that the phrase ‘any obligations it may have entered into’ could not but refer to anything other than obligations which were contained in investment contracts, since states do not usually enter into investment agreements with other states. The treaty clause is thereby ‘specific’, not broad or general, for investment contracts after all contain specific rights. The words ‘entered into’ likewise suggested an intention to include specific commitments, rather than general commitments undertaken by way of legislative acts. As the tribunal then put it:

… a clause that is readily capable of being interpreted in this way and which would otherwise be deprived of practical applicability is naturally to be understood as protecting investors also with regard to contracts with the host state generally in so far as the contract was entered into with regard to an investment.

42 Noble Ventures, ICSID Case No. ARB/01/11, Award, 12 October 2005, paras. 46–62.
43 Id., para. 50.
45 Noble Ventures, ICSID Case No. ARB/01/11, Award, 12 October 2005, para. 51.
46 Id. 47 Id. 48 Id., para. 52.
Analysing this ‘plain meaning’ approach  According to the *Noble Ventures* tribunal, therefore, one should look closely at the language and formulation of the specific clauses. The tribunal offered a useful analysis of the different forms of treaty language in prior cases. It considered that the *Salini* tribunal had reached the correct result since the words ‘shall create and maintain in its territory a legal framework apt to guarantee to investors the continuity of treatment, including the compliance, in good faith, of all obligations’ simply did not suggest the existence of an umbrella clause. 49 According to the *Noble Ventures* tribunal, the word ‘guarantee’ in the BIT in *SGS v. Pakistan* suggests a similar reading. What Pakistan had undertaken to do was to take the requisite steps to protect contractual commitments under its municipal law. The clause in the Switzerland–Pakistan BIT therefore contained a general, rather than a specific, obligation. 50

In contrast, however, the treaty clause in *SGS v. Philippines* stated that each party ‘shall observe any obligation it has assumed with regard to specific investments made by investors of the other party’. The wording of the clause makes the breach of the investment contract itself a treaty violation. 51 In particular, the *Noble Ventures* tribunal observed the ‘directness’ of the reference in the Switzerland–Philippines BIT umbrella clause to investment contracts – i.e. ‘any obligation it has assumed with regard to specific investments’. In *Noble Ventures*, the US–Romania BIT’s reference to ‘any obligation’ the host state ‘may have entered into’ was considered to be equally direct, or explicit, in its reference to all forms of investment contracts because of the words ‘obligation’ and ‘entered into’. 52

This ‘plain meaning’ approach was subsequently adopted by the tribunal in *Eureko v. Poland* which also cited the tribunal’s view in *SGS v. Philippines* that the treaty in that case ‘means what it says’ and should be given its ‘plain meaning’. 53 This approach has the benefit of simplicity if not elegance. Even if it cannot settle all cases of doubt, it does present a useful device for weeding out such generally worded clauses which

49 Id., para. 57.  
50 Id., para. 58.

51 Although the tribunal in *SGS v. Philippines* had also considered the clause in the Swiss–Pakistan BIT “arguably similar” to that in the Swiss–Philippine BIT; *SGS v. Philippines*, paras. 97, 199; discussed in Sinclair, “The Umbrella Clause Debate”, 286.

52 Even if the tribunal’s choice of words in its reference to the clause as one falling into the category of “the most general and direct formulations” is an unhappy one. See para. 60.

53 *Eureko v. Poland*, paras. 256, 258. However, the *Eureko* tribunal criticised the Award in *SGS v. Pakistan*, Id., para. 257.
cannot, on their proper construction, be taken to qualify as umbrella clauses at all. Clearly, clauses which undertake to ‘create and maintain’ in the host state’s territory an appropriate ‘legal framework’ cannot qualify as umbrella clauses.

‘Plain meaning’ versus ‘sweeping and unqualified meaning’
But what about clauses which, like the clause in the Swiss–Pakistani treaty, require that the host State ‘shall constantly guarantee the observance of the commitments it has entered into’? While the Noble Ventures tribunal considered such a ‘guarantee’ of ‘observance’ to be substantially similar to the commitment in the BIT in Salini (i.e. merely guaranteeing the existence of effective domestic laws for the continued enforcement of legal commitments), the tribunal in Eureko saw no essential difference between a ‘guarantee of observance’ and an ‘undertaking to observe’ a host state’s commitments under the traditional Abs/Shawcross formulation.

The reasoning of the tribunal in SGS v. Pakistan had been especially complex. While the tribunal rejected the umbrella clause, as the subsequent Noble Ventures tribunal apparently would have done, it did so for entirely different reasons. Like the Eureko tribunal, the SGS v. Pakistan tribunal took the Swiss–Pakistani clause seriously; so seriously that it reasoned that treaty clauses requiring the host state to ‘constantly guarantee the observance of the commitments it has entered into’ would not be limited to the observance of contractual obligations. It did not view the words ‘constantly guarantee’ and ‘commitments entered into’ as qualifying words at all. Rather, they would be ‘so far-reaching in scope, so automatic and unqualified and sweeping in their operation, and so burdensome in their potential impact upon a Contracting Party’ that ‘clear and convincing evidence’ would be required to show such actual treaty intent.\(^\text{54}\) An unlimited number of state contracts would be protected, rendering other treaty protective standards ‘substantially superfluous’.\(^\text{55}\) Freely negotiated contractual forum selection clauses would be

\(^{54}\) SGS v. Pakistan, ICSID Case No. ARB/01/13, Decision on Objections to Jurisdiction, 6 August 2003, paras. 166–173.

\(^{55}\) However, umbrella clauses that only apply to specific commitments are unlike other treaty standards in a BIT which are general in nature. The latter being general rather than specific are not thereby rendered superfluous by the existence of an umbrella clause. See Sornarajah, International Law on Foreign Investment, 3rd ed., 215.
nullified, while the treaty clause was not even located together with the other protective treaty standards. These factors led the tribunal to doubt, as a matter of construction, that the treaty parties intended to create such a ‘sweeping and unqualified’ effect.

Problems of construction are especially fraught. Yet, the true cause of all this confusion is not that it involves the problem of treaty construction. The true cause might well be thought to lie in Gaillard’s and Weil’s invocation of that phantasm – the ‘internationalisation’ of the entire underlying contract by an umbrella clause.

**El Paso: the myth of the ‘internationalised’ contract lurks still**

There the matter could have ended; it was all simply a confusion over the construction of different terms, but for the fact that the tribunal in *SGS v. Philippines* also viewed the Award in *SGS v. Pakistan* to have been fundamentally mistaken. According to the tribunal in *SGS v. Philippines*, an umbrella clause need not mirror, transform, elevate or internationalise the underlying contract at all. In the words of the *SGS v. Philippines* tribunal, umbrella clauses address ‘not the scope of the commitments entered into with regard to specific investments, but the performance of these obligations once they are ascertained’. An umbrella clause ‘does not convert the issue of the extent or content of such obligations into an issue of international law’. Similarly, the *Noble Ventures* tribunal had considered it unnecessary to answer the question whether ‘any’ breach of ‘any obligation’ would perfectly assimilate to a treaty breach.

The odd theory that umbrella clauses were capable of internationalising entire underlying contracts had led the tribunal in *SGS v. Pakistan* to apply a strict evidentiary presumption against umbrella clauses. In this manner, a boundless theoretical view became a justification for prudence in respect of a practical legal issue, resulting in a strong presumption against the very existence of umbrella clauses.

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56 See the discussion in “Problems with the contractual forum selection clause” section.


58 *Noble Ventures*, ICSID Case No. ARB/01/11, Award, 12 October 2005, para. 61.


60 *SGS v. Pakistan*, ICSID Case No. ARB/01/13, Decision on Objections to Jurisdiction, 6 August 2003, para. 173 (“The Tribunal is not saying that States may not agree with each other in a BIT that henceforth, all breaches of each State’s contracts with investors of the other State are forthwith converted into and to be treated as breaches of the BIT. What the
But then came *El Paso v. Argentina*, a case in which Professor Sornarajah served as an expert, only to re-confirm this original theoretical conceit. Like *SGS v. Pakistan*, the *El Paso* tribunal concluded that the phrase ‘any obligations’ is so broad that it could include the breach of any obligation by the host state, thereby rendering the whole treaty superfluous. According to the tribunal, ‘the smallest obligation of a state with regards to investment falls to be protected by the BIT and could give rise to an ICSID obligation’. The tribunal in *El Paso* then criticised the incoherence of the view taken in *SGS v. Philippines*, which, as we saw earlier, had considered that while the contractual breach may be brought as a treaty claim under the umbrella clause, the contractual obligations themselves are governed separately by ordinary contractual principles. According to the *El Paso* tribunal, this would require investment tribunals to rule on contractual claims.

It is difficult to understand the *El Paso* tribunal’s reservation. After all, a tribunal can engage in contractual analysis if the parties have mandated the tribunal to do so, and even in the absence of party agreement, various institutional rules (e.g. ICSID and UNCITRAL) typically accord the tribunal the discretion to apply domestic contract law either directly or

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Tribunal is stressing is that in this case, there is no clear and persuasive evidence that such was in fact the intention of both Switzerland and Pakistan in adopting Article 11 of the BIT”.

61 *El Paso v. Argentina*, ICSID Case No. ARB/03/15, Decision on Objections to Jurisdiction, 27 April 2006.

62 *Id.*, para. 76. No attempt was made to distinguish between the treaty protections that are of general application and umbrella clauses, which apply only to specific commitments.

63 *El Paso v. Argentina*, ICSID Case No. ARB/03/15, Decision on Objections to Jurisdiction, 27 April 2006, paras. 76–77. Curiously, the *El Paso* tribunal appeared to have considered that *Eureko* and *Noble Ventures* supported its view. But see, however, *Eureko*, op. cit., para. 256, and *Noble Ventures*, ICSID Case No. ARB/01/11, Award, 12 October 2005, para. 61. *El Paso*’s (and *SGS v. Pakistan*’s) theory of the internationalised contract was, however, shared by other recent Awards. See *BIVAC v. Paraguay*, ICSID Case No. ARB/07/9, Decision on Jurisdiction, 29 May 2009, para. 142 (“it must have imported into the BIT all of the obligations owed … under the Contract”); *PanAm v. Argentina*, Decision on Preliminary Objections, ICSID Case No. ARB/03/13, ARB/04/8, para. 105. I do not read *SGS v. Paraguay*, ICSID Case No. ARB/07/29, Decision on Jurisdiction, 12 February 2010, to suggest such internationalisation. In fact, the tribunal went to great lengths to show that it did not need to decide whether the claims were merely contractual and not based upon treaty; which under a theory of the internationalised contract would be one and the same. In any event, the tribunal considered that the umbrella clause operated independently of the underlying contract was not solely reliant upon the contents of the contract and may in fact have been broader in scope than the contract; see *Id.*, paras. 125–142. Likewise, in *Duke Energy v. Ecuador*, ICSID Case No. ARB/04/19, Award, 18 August 2008, the tribunal had left the question of internationalisation open – see *Id.*, para. 319.
by first applying the choice of law rules of the appropriate domestic legal system in order to determine the proper law of the contract.\textsuperscript{64}

If \textit{El Paso} is somehow correct, the most ordinary contractual commitment could become an investment-treaty commitment. In this way, the \textit{El Paso} tribunal saw a need to discuss the proliferation of devices which have been intended to limit the supposedly wide effect of umbrella clauses.\textsuperscript{65}

\textbf{Distinguishing commercial from investment commitments}

The \textit{El Paso} tribunal cited a wide variety of approaches, starting with that adopted by the tribunal in \textit{Joy Mining v. Egypt}.\textsuperscript{66} That latter dispute had concerned the potential application of an umbrella clause in the UK–Egypt BIT to certain performance guarantees regarding the proper functioning of equipment used at an Egyptian phosphate mine. The Egyptian agency, IMC, had alleged defective performance. Joy Mining submitted the dispute to ICSID arbitration. Egypt’s argument was that this was a purely commercial dispute involving the sale of equipment, paid for by a confirmed irrevocable letter of credit, and that Joy Mining had therefore already been paid in full. As for the performance guarantee, it too was an ordinary commercial agreement and Egypt had not after all drawn on the guarantee. According to Egypt, the dispute only concerned its refusal to release the guarantees according to the agreed schedule because of the existence of the dispute about Joy Mining’s allegation of mismanagement by Egypt’s IMC, while IMC alleged that it had been supplied with defective equipment.

All of this, according to Egypt, has nothing whatsoever to do with an ‘investment’. Joy Mining, however, contended that a guarantee which represents 97% of the contract price amounts therefore to an ‘investment’.

The tribunal did not automatically preclude sales disputes from becoming investment disputes, but held that such situations would be

\begin{itemize}
  \item \textsuperscript{65} Professor Jeswald Salacuse has classified the cases into those which support the plain meaning approach and others which “seem to be influenced by the consequences to states and to the arbitral system of giving too broad an interpretation to the clause”; Salacuse, \textit{Law of Investment Treaties}, 280.
  \item \textsuperscript{66} \textit{Joy Mining v. Egypt}, ICSID Case No. ARB/03/11, Award on Jurisdiction, 6 August 2004.
\end{itemize}
exceptional. This, incidentally, reflects a long-standing view advanced by F.A. Mann: ‘difficulties may arise in the event of the sale of goods’, Mann once wrote, but ‘where a very expensive machine or ship is supplied, this may well constitute an “investment”’. According to the tribunal in Joy Mining, a dispute over a performance guarantee was, however, an inherently commercial dispute, because there was only a peripheral relationship with the underlying ‘investment’. The tribunal presided over by Professor Francisco Orrego-Vicuna considered that:

Disputes about the release of bank guarantees are a common occurrence in many jurisdictions and the fact that a State agency might be a party to a Contract involving a commercial transaction of this kind does not change its nature. It is still a commercial and contractual dispute …

The tribunal went on to explain that had there been an investment, the purported umbrella clause was in any case akin to that in SGS v. Pakistan – ill-placed in the treaty and thereby lacking ‘prominence’. As for the language of the clause, Article 2(2) of the BIT had stated in a final sentence at the end of a long paragraph 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.

In any event, the nature of the underlying contract now become a key issue in the evolving jurisprudence on umbrella clauses. The SGS cases had concerned contracts for pre-shipment inspection services, while the Noble Ventures and Eureko cases had concerned the terms of share purchase agreements which had been employed as the preferred vehicle under various national privatisation policies. Much now turns upon what a tribunal, going through the facts, understands by an ‘investment’.

Notice, however, that had the tribunal in Joy Mining adopted the internationalisation theory, there would have been no distinction between commercial and investment disputes. In this way, the tribunal’s
view is at least consistent with the rejection of internationalisation\textsuperscript{72} and is on that basis sound. Suppose, we had a construction contract in which the host State is the employer and the contractor alleges that it is an investor; can one simply say that the breach of a payment clause by virtue of a small, delayed payment would automatically amount to a treaty breach? In contrast, the unlawful repudiation or termination of a contract presents a clearer case of the breach of the umbrella clause where the very existence of the contract might be said to constitute the whole basis of the investor’s investment.

Although phrases like ‘any commitment’ suggest a wider meaning, they are typically also qualified by words such as ‘in relation to investments’. One might then, as the El Paso tribunal did subsequently, look to the definitions clause in the treaty. This would still be entirely consistent with a ‘plain meaning’ approach to umbrella clauses. Another way may be to rely upon the ‘Salini criteria’ derived from ICSID jurisprudence.\textsuperscript{73}

The El Paso tribunal canvassed a third method, to which we now turn. It involves distinguishing between a host state acting in its sovereign capacity and in a merchant capacity.\textsuperscript{74} It is suggested, according to this third method of limiting the effect of umbrella clauses, that purely private acts of the host state have nothing to do with the host state’s investment commitments.

**Acta jure imperii**

The El Paso tribunal cited CMS v. Argentina, which had adopted another device for containing the effect of umbrella clauses.\textsuperscript{75} CMS had bought into a new company, TGN, which had been granted a gas transportation licence. The dispute concerned the tariff adjustment formula for gas transportation after Argentina’s dismantlement of the tariff regime in the wake of the 1999 Argentine financial crisis. Article II(2)(c) of the US–Argentina BIT stipulated that the Contracting Parties: ‘shall observe any obligation it may have entered into with regard to investments’. According to the tribunal (the President was, again, Professor Orrego-Vicuna):\textsuperscript{76}

\textsuperscript{72} However, we will never know for sure as the arbitrator also rejected the clause as an umbrella clause.


\textsuperscript{74} El Paso, para. 79.

\textsuperscript{75} The Award was subsequently annulled but not, I think, on this point.

\textsuperscript{76} CMS v. Argentina, ICSID Case No. ARB/01/8, Decision on Annulment, 25 September 2007, para. 299.
Purely commercial aspects of a contract might not be protected by the treaty in some situations, but the protection is likely to be available when there is significant interference by government or public agencies with the rights of the investor.

Notice that the Tribunal’s requirement of ‘significant interference by government or public agencies’ is presumably only a necessary but insufficient requirement. In *Joy Mining*, the tribunal there had said that ‘the fact that a State agency might be a party to a Contract involving a commercial transaction of this kind does not change its nature’, and that the nature of the underlying contract in *Joy Mining*, being purely commercial, precluded its treatment as an investment.\(^77\)

The *El Paso* Award and the Award in *Joy Mining* are now cited as authority for the proposition that states ‘entering into such obligations must be acting as sovereigns and not as merchants’.\(^78\) Such a view at least accommodates the internationalisation theory. The argument would go something like this. The contract is internationalised, but an ordinary commercial breach of the contract would not fall within the scope of the umbrella clause, as opposed to a breach by the sovereign acting in its sovereign capacity.

The effort to distinguish between sovereign and merchant acts has not met with universal acceptance. It had been argued by the Respondent in *SGS v. Paraguay*, but the argument was dismissed by that tribunal, which considered that where the plain language of the treaty does not distinguish between a governmental or other act, then no such distinction ought to be imposed.\(^79\) For the sake of completeness, it is also worth mentioning that in *El Paso* and *Vivendi*, it had been said that the sovereign host state at least possesses an international legal personality which an independent state agency may not possess.\(^80\) Yet, quite arguably, no reliance can be placed on...

\(^{77}\) *Joy Mining v. Egypt*, ICSID Case No. ARB/03/11, Award on Jurisdiction, 6 August 2004, para. 79.


\(^{80}\) *Vivendi*, Annulment, para. 96; *El Paso*, para. 79.
this factor where the act of the agency is, in any event, attributable to the state under the normal rules of state responsibility.81

Overlap with fair and equitable treatment and other substantive treaty standards

However, the El Paso tribunal itself concluded, ultimately, that an umbrella clause’s scope ought to be limited by the existence of a concurrent violation of some other substantive treaty standard. Where there has been such a concurrent breach which is attributable to the state, the jurisdiction of the investment tribunal will be established.82 This highlights a new front in the debate – the potential operation of FET clauses as ‘de facto umbrella clauses’.83 This link with the FET standard was also drawn in SGS v. Paraguay, and in EDF v. Argentina, the tribunal observed that the FET clause and the umbrella clause operated ‘in tandem’.84

Problems with the contractual forum selection clause

The rules of treaty interpretation

These various ways of limiting the effect of umbrella clauses which we have discussed stem from the ‘public international law side’ of the analysis. Other tools have also emerged from the ‘contractual side’ of the equation. The most serious challenge from the contractual side concerns the effect which ought to be given to the contractual forum selection clause. As the SGS v. Pakistan tribunal saw it:85

A third consequence [of sweeping umbrella clauses] is that an investor may, at will, nullify any freely negotiated dispute settlement clause in a State contract. On the reading of Article 11 urged by the Claimant, the benefits of the dispute settlement provisions of a contract with a State also

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82 El Paso v. Argentina, ICSID Case No. ARB/03/15, Decision on Objections to Jurisdiction, 27 April 2006, paras. 82, 84.
83 Laird et al., International Investment Law and Arbitration, 150.
85 SGS v. Pakistan, ICSID Case No. ARB/01/13, Decision on Objections to Jurisdiction, 6 August 2003, para. 168. The reference to “differing legal orders” is interesting, and casts some doubt on the tribunal’s complete adherence to a theory of internationalisation.
a party to a BIT, would flow only to the investor. For that investor could always defeat the State’s invocation of the contractually specified forum, and render any mutually agreed procedure of dispute settlement, other than BIT-specified ICSID arbitration, a dead letter, at the investor’s choice ... The Tribunal considers that Article 11 of the BIT should be read in such a way as to enhance mutuality and balance of benefits in the inter-relation of different agreements located in differing legal orders.

However, recall the Vivendi Annulment Committee’s view that, although the sentiment expressed by the SGS v. Pakistan tribunal is appealing, contractual clauses cannot extinguish an investor’s treaty rights as a matter of international legal principle.

In treaty terms, the circumstances in which contractual rights might extinguish or affect treaty rights would require the contractual right to supersede, amend or at least condition the interpretation of the treaty right. From the perspective of the hierarchy of legal norms, it is difficult to see how this could occur unless the contractual right itself somehow came to possess the status of international law – i.e. unless it is ‘elevated’ to the level of a treaty right – failing which a domestic law contractual right cannot serve as an excuse for the breach of a treaty right.86

There are ways under the rules of treaty interpretation by which BIT rights may be conditioned by contract. One thing seems clear, however; the contract cannot be said to constitute a ‘subsequent agreement’ between the Contracting Parties under Article 31(3)(a) of the Vienna Convention on the Law of Treaties of 1969 (VCLT) because the investment contract is only a contract with the foreign investor, not its home state.87 However, under Article 31(3)(b), a ‘subsequent practice which establishes the agreement of the Parties’ could affect the reading of a treaty right. One would have to argue that the conclusion of the investment contract is a subsequent practice of the host state, one which the home state accepts implicitly, and that the home state’s acceptance establishes – either alone or in combination with other facts – the ‘agreement’ of the treaty parties themselves. In such a case, the contractual forum selection clause would, as a matter of the proper

86 There was the suggestion, to the contrary, that a subsequent contract would simply supersede the BIT, but it is difficult to understand how that could occur unless, as I have argued here, the contract itself is elevated to the level of a subsequent international agreement; see BIVAC, Decision on Jurisdiction, 29 May 2009, para. 146; discussed also in SGS v. Paraguay, Decision on Jurisdiction, 12 February 2010, para. 178.
87 It is well known that the home state in SGS v. Pakistan subsequently expressed dissatisfaction with the tribunal’s construction of Article 11 of the Switzerland–Pakistan BIT.
interpretation of the BIT, be able to condition the reading of a BIT umbrella or arbitration clause or both.

A second possible way, under Article 31(3)(c) of the VCLT, may be if the contract had become internationalised.88 It could then become a ‘rule of international law’, which is ‘relevant’ and ‘applicable’ to the state parties, and, therefore, ought to be taken into account in the interpretation of the BIT. The very difficult idea that such a contract is also ‘applicable’ to the home state would have to be argued further.

The view in SGS v. Philippines

The problem occurs because the BIT stipulates recourse to investment arbitration.89 In SGS v. Philippines, the tribunal upheld the umbrella clause while, at the same time, upholding the contractual forum selection clause. It pays to attend to how this occurs in the tribunal’s view. The tribunal treated the contractual forum selection clause as a form of lex specialis, because the BIT arbitration clause did not refer to any specific investment or contract, while the contractual forum selection clause in fact did.90

This approach drew criticism from the El Paso tribunal, as well as in academic commentary.91 The El Paso tribunal asked how the forum selection clause could have survived if the umbrella clause had already ‘overridden’ the contract.92 The dissenting arbitrator in SGS v. Philippines, Professor Crivellaro, offered one possible answer – the BIT having been concluded after the contract expanded the rights of the investor by giving the investor a choice of a further forum in addition to the options stipulated in the contractual forum selection clause.93

88 In BIVAC v. Paraguay, the tribunal reasoned that, once all the terms of the contract are elevated to treaty status, then the forum selection clause must – as with any BIT provision – be given effect to within that treaty setting; ICSID Case No. ARB/07/9, Decision on Jurisdiction, 29 May 2009, paras. 142–158, cited in SGS v. Paraguay, Decision on Jurisdiction, 12 February 2010, para. 172.
89 For the separate regimes of treaty and contract, see again Vivendi, Annulment, ICSID Case No. ARB/97/3, Decision on Annulment, 3 July 2002, paras. 95, 96.
90 SGS v. Philippines, ICSID Case No. ARB/02/6, Decision on Jurisdiction, 29 January 2004, para. 141.
92 El Paso v. Argentina, ICSID Case No. ARB/03/15, Decision on Objections to Jurisdiction, 27 April 2006, para. 76.
93 SGS v. Philippines, ICSID Case No. ARB/02/6, Decision on Jurisdiction, 29 January 2004, Declaration of Arbitrator Crivellaro. 2–4, 10.
But, what if the contract came after the BIT? There is no reason to suppose that in such event the umbrella clause could not, on its proper construction, direct the tribunal to the contractual forum selection clause itself by way of *renvoi*.\(^{94}\) In fact, the reasoning in *SGS v. Philippines* that the contractual forum clause amounts to *lex specialis* might already suggest such an approach. As we have seen, the forum selection clause could also be given effect, notwithstanding the BIT’s provision for investor-state arbitration, if in the circumstances the contractual right even if it did not supersede or amend the treaty right has nonetheless conditioned the interpretation of the latter. This, as we have already seen (in the section “The rules of treaty interpretation”) might be done by applying the treaty interpretation rules under Article 31(3)(b) or (c) of the VCLT.\(^{95}\)

**The doctrine of privity of contract**

Another challenge from the contractual side of the equation has emerged in the form of the privity doctrine. Gallus has shown that there are two aspects to the problem. The first occurs where a subsidiary that the state has harmed was not a party to the contract, while the second occurs

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\(^{94}\) In other words, if the treaty clause, properly interpreted, points to the application of the forum selection clause by way of *renvoi*, or if on its plain meaning the umbrella clause is taken not to have been intended to interfere with the contractual balance between the investor and the host state (thereby presenting both investor and state equal options in respect of forum selection). The fear of an expansion of the scope of treaty commitments remains, however, and this view could be treated as just another species of internationalisation. Conceptually, it is different from the elevation or internationalisation theory because the tribunal will employ ordinary forms of contractual analysis to the forum selection clause itself.

\(^{95}\) We should beware that the problem also concerns the enforcement of such clauses by *municipal* courts. It is not entirely unimaginable that some courts, such as the English courts, may be slow to interfere with investment arbitration, especially ICSID arbitration particularly due to the perception that the ICSID process is “self-contained”. Even matters connected with investment arbitration are justiciable (*Occidental v. Ecuador* [2005] EWCA Civ. 116, esp. paras. 41–42 *per* Mance L.J.), but there is *dicta*, which suggests that where the matter is properly remitted to the jurisdiction of an ICSID tribunal, special considerations raised by the ICSID Convention’s largely self-contained arbitration procedures could arise (*E.T.I. Euro Telecom v. Bolivia* [2008] EWCA Civ. 888 at paras. 99–109 *per* Collins L.J.). Conversely, a tribunal is bound to take an investment treaty right seriously; see *SGS v. Paraguay*, Decision on Jurisdiction, 12 February 2010, para. 172 (“risk of failing to carry out its mandate”), citing (at para. 171) *Vivendi*, Annulment, ICSID Case No. ARB/97/3, Decision on Annulment, 3 July 2002, para. 112.
where a sub-state entity responsible for the breach was not party to the contract entered into by the host state.96

Beginning with the first,97 the CMS Annulment Committee had reasoned that where the treaty clause itself allows the parent to enforce the rights of a subsidiary the privity issue is irrelevant.98 Much will depend upon whether a tribunal would treat the treaty analysis separately from the contractual analysis, as the SGS v. Philippines tribunal apparently did and which the El Paso tribunal rejected.

As for the second aspect, the problem may be overcome where the sub-state entity’s actions are attributable to the host State under the international law rules of state responsibility.99

There is a broader objection to the privity doctrine where the underlying contract is considered to have become elevated or internationalised. Once all the contractual terms are elevated to the status of treaty terms, it becomes difficult to see how any room is left for contractually based limitations such as the privity doctrine. There appears neither room nor need left for any contractual analysis. One would have to argue that there is an equivalent treaty doctrine which applies to internationalised contracts.

**The problem with elevating or internationalising the contractual terms under an umbrella clause**

At bottom, however, the idea that all the contractual terms could become elevated or internationalised by an umbrella clause is problematic. Sornarajah’s complaint has been that ‘[t]he process of this transformation has not been explained’.100 As he put it in his Opinion in El Paso v. Argentina:101

> Being domestic contracts, contracts of foreign investment create obligations only in domestic law. It is without doubt that, through the use of appropriate language, the rights so created can be lifted up and subjected to an international regime of protection. But, the extent of those rights

97 See Id., 159–162 for a survey of the split authorities.
98 CMS v. Argentina, ICSID Case No. ARB/01/8, para. 95.
must depend on domestic law ... they can be protected only to the extent that they exist in domestic law.

F.A. Mann’s view, on the contrary, was that we should turn to ‘the commercial law of nations’, which drew an unhappy retort from Sornarajah.\textsuperscript{102} In essence, such reliance upon the ‘low order sources of international law’ is a retreat to the realm of private law analogies in the absence of a formal, as opposed to only a material, source of international legal justification.

The greatest difficulty may not be how internationalisation occurs, but what it means to admit the theory of the internationalised contract. In the umbrella clause debate, it presupposes that treaty law has doctrines that are equivalent to domestic contract law. Even outside the umbrella clause debate, if we were simply to rely on some low-order source such as Mann’s ‘commercial law of nations’ as the basis for saying that a contract has become an ‘internationalised’ contract, that would almost presuppose that private international law practice has become irrelevant.

Conclusion

According to Sornarajah, a principal difficulty concerns the need to, first, ascertain the theoretical implications of umbrella clauses.\textsuperscript{103} This chapter has tried to do that by showing how the extent or degree to which umbrella clauses might expand host state commitments depends ultimately upon whether or not we adopt the theory of the ‘internationalised contract’.

I have discussed how SGS v. Philippines gave effect to the umbrella clause without elevating all the contractual commitments to some unexplained treaty status. That Award struck an intermediate position, but it was fiercely criticised by the El Paso tribunal, whose analysis was based upon the earlier view taken in SGS v. Pakistan that the contractual commitments would be elevated – a view which both the El Paso and Pakistan tribunals considered to be a logical consequence of upholding umbrella clauses.

Tribunals have adopted the ideas of elevation or internationalisation, or what Gaillard calls the mirror theory, as a result of certain influential scholarly writings in the field. To this extent, we might say that internationalisation has been the dominant view all along. However, an umbrella clause could – as this chapter has tried to argue – simply

\textsuperscript{102} Sornarajah, “Myth”, 199, 201, 202.
require, as a matter of plain treaty construction, that the breach of some contractual commitments should be treated as breaches of the overlying BIT but that other contractual breaches should not. The SGS v. Philippines tribunal had explained this view forcefully by stating that an umbrella clause ‘does not convert the issue of the extent or content of such obligations into an issue of international law’.

The illustration given earlier in this chapter is that of a construction contract in which delayed payment by the host state could be treated as a simple contractual breach but that unlawful termination of the contract itself, which is the basis of the whole investment, would prima facie rise to the level of a treaty breach.

Despite the dominant scholarly view, the arbitral jurisprudence today contains strong suggestions that an umbrella clause should be construed as if it were just another treaty clause, does not require always the conversion of every contractual term into a treaty term, that the distinction between treaty and contract should be observed and that in applying umbrella clauses one ought to focus only upon whether the breach of the specific contractual or other commitment amounts also to a treaty breach.

Taking such an approach would neither result in a broader nor narrower reading than what ordinary treaty construction would require. If this plain view is adopted, there would also be less urgency in seeking to limit the operation of umbrella clauses.

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105 This is the fourth of James Crawford’s four-fold classification; “Treaty and Contract”, 368; see also A.R. Sureda, Investment Treaty Arbitration: Judging under Uncertainty (Cambridge: CUP, 2012), 33.

106 In some cases, a difficult question might arise about the need to imply elements of the host state’s regulatory framework into the terms of the contract. In such cases, the contention is that subsequent regulatory changes have breached implied contractual terms. According to Sornarajah, in his Opinion in El Paso, Legal Opinion of M. Sornarajah in El Paso v. Argentina, ICSID Case No. ARB/03/15, 5 March 2007, para. 96, the tribunal in LG & E v. Argentina, ICSID Case No. ARB/02/1, Decision on Liability, 3 October 2006, had (erroneously) read the host state’s regulatory provisions into the contract. If so, in such cases, it is not the treaty commitments of the host state, which have necessarily been expanded, but the host state’s contractual commitments. Similarly, the question would have less to do with the construction of the umbrella clause as such, once it is accepted that the treaty clause encompasses breaches of contractual commitments. With respect, however, it is not obvious that this was necessarily what had transpired in LG & E. Rather, Argentina had made promises to which it bound itself under general legislation or regulations, and these legally binding promises fell within the scope of the ‘obligations’ which the BIT umbrella clause sought directly to protect. It was the Respondent itself, Argentina, which had contended that the promises were merely domestic contracts. See Id., paras. 164–175.
great difference ultimately in practice, but as Sornarajah once observed, it is important to be clear about what we are talking about.

Since some of the factors relied upon to limit the scope of umbrella clauses – such as asking whether a sovereign act was involved, or whether the host state government was itself party to the contract – might still play an evidential role in determining whether the particular contractual breach ought to be considered a breach of the treaty in light of the particular language of the umbrella clause.