



UPPSALA
UNIVERSITET

Department of Law
Spring Term 2019

Master Programme in Investment Treaty Arbitration
Master's Thesis 15ECTS

Title

Subtitle

"Convergence or divergence: recent trends in the
application of the umbrella clauses"

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Introduction

The clause is also known by "pacta sunt servanda clause", "sanctity of contract clause", "respect clause", "observation of undertaking clause", "mirror clause", or umbrella clause"¹

An umbrella clause has many definitions but mainly it is a "provision in an investment protection treaty that guarantees the observance of obligations assumed by the host state vis-à-vis the investor"².

In simple terms, the umbrella clause is a phrase mentioned in the bilaterally and multilateral treaties to establish the principle of the host state responsibility for the breach of any obligations towards the investor, So that any breach, even if contractual by the state, would be a breach of the treaty of investment protection³.

The first attempt to promote contractual breaches into a treaty breach was upon the Iranian Government Issuance the law of 1951 for nationalization all the operations regarding the oil sector in Iran. Anglo-Iranian Oil Company (AIOC) was in that time a British oil company who had a long term concession agreement with the Iranian republic and was directly affected by the nationalization law of 1951.

Other states who has Interests in the oil sector in Iran tried to persuade the Iranian government to reconsider the nationalization act of 1951 to no avail. Also Britain tried to make claims against Iran in front of the International Court of Justice "ICJ" which failed. Until the Iranian government was changed by a coup and the oil companies started to renegotiate their agreements with the Iranian government to make sure that what happened won't happen again.

1 - OECD, Interpretation of the Umbrella Clause in Investment Agreements, Working Papers on International Investment, No. 2006/3, October 2006, available at: www.oecd.org

2 – principles of international investment law , by R.Dozler and . Second edition p.166

3- "Umbrella clause and the privity of contract by the author p.2

Lauterpacht⁴ at that time advised the oil companies to renegotiate their agreements with the Iranian government and to include the agreement an umbrella clause that every breach for the agreement is a breach to the treaty between Iran and the United Kingdom. But Lauterpacht's suggestion was not considered⁵.

Those suggestions appeared again on 1956 when a group of oil companies was responsible for constructing a trunk pipe line from Iraq to the Mediterranean Sea and again those suggestions were not considered⁶.

In 1958 the Abs-Shawcross Draft Convention was submitted by Dr. Herman Abs⁷ and Sir Hartley Shawcross⁸ and developed by them for the protection the foreign investor. Both dr.Herman and Sir Shawcross were writing at the same subject individually but their combined draft convention had a similar formulation to the umbrella clauses in modern BITs. Article II of the Abs-Shawcross Draft Convention stated:

“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.”⁹

This draft raised many questions and discussions. Whether this clause covers the unilateral violations by the host state and whether the clause change the nature of the contractual internal law obligations into obligations under international law. And also some commentary said that no state will accept those terms¹⁰.

It was not until 1959 when the first umbrella clause ever was included in the bilateral investment treaty between Germany and Pakistan. Article 7 of this BIT states:

4- Sir Hersch Lauterpacht QC was a Polish-British lawyer and judge at the International Court of Justice

5 - The impact of investment treaties on contracts between host states and foreign investors by, Jan Ole Voss p.224

6- Ibid p.224

7 - a German banker who was a member of the board of directors of Deutsche Bank from 1938 to 1945.

8 - a British barrister and politician and the lead British prosecutor at the Nuremberg War Crimes tribunal

9 - The impact of investment treaties on contracts between host states and foreign investors by, Jan Ole Voss p.226

10 – Ibid p.226

"Either Party shall observe any other obligation it may have entered into with regard to investments by nationals or companies of the other Party"

And since that date, many developed countries included umbrella clauses in their BITs. In an OCED study it shows that states like: Japan, Australia and Canada kept the usage of the umbrella clause at their BITs at the minimum, while other states like Germany, UK and Netherlands often used the umbrella clause in their BITs. While the US in its Model BIT of 2004 contained an umbrella clause, this has change in the recent Model of the US BIT.¹¹

As an example for umbrella clauses in BITs, the umbrella clause in Denmark – Cuba BIT 2001 article 3 which states:

"Each Contracting Party shall observe any obligation it may have entered into with regard to investment of investors of the other Contracting Party"

Also article 2 of Sweden-Bosnia Herzegovina BIT 2000 which states :

"Each Contracting Party shall observe any obligation it has entered into with investors of the other Contracting Party with regard to their investment"

Also article 15 of Czech Republic-Singapore BIT 1995 which states:

"Each Contracting Party shall observe commitments, additional to those specified in this Agreement, it has entered into with respect to investments of the investors of the other Contracting Party. Each Contracting Party shall not interfere with any commitments, additional to those specified in this Agreement, entered into by nationals or companies with the nationals or companies of the other contracting Party as regards their investments"

11 - US Model BIT 2012

After the first umbrella clause was included on 1959, it became a trend and kept included in other BITs typically in an almost identical formulation "Each Contracting Party shall observe any other obligation it has assumed with regard to investments by nationals or companies of the other Contracting Party in its territory"

And was not until 2003 when the umbrella clause attracted the attention of the legal scholars. By that time there was an agreement upon the jurisprudence regarding the umbrella clause function which was :

"These provisions seek to ensure that each Party to the treaty will respect specific undertakings towards nationals of the other Party. The provision is of particular importance because it protects the investor's contractual rights against any interference which might be caused by either a simple breach of contract or by administrative or legislative acts, and because it is not entirely clear under general international law whether such measures constitute breaches of an international nature or not"¹²

In general it was expected to have some complications regarding the application of the umbrella clause by the arbitral tribunals but what happened was applying this clause became one of the most controversial topics in international treaty investment law.

Those complications have emerged clearly when the Two ICSID tribunals "SGS vs. Pakistan & SGS vs. Philippines" had to interpret the umbrella clause in Switzerland – Pakistan BIT 1995 and Switzerland – Philippines BIT 1997. Although the wording of the umbrella clause in the two Bits is almost identical, the two tribunals reached Contradictory results. While the first tribunal " SGS vs. Philippines" interpreted the umbrella clause in the BIT a broad interpretation which include commercial breaches to the jurisdiction of the forums of the treaty breaches , the other tribunal " SGS vs. Pakistan" did not agree with them. And their interpretation of the clause did not give the investor the right to resort the treaty breaches forums regarding the commercial breaches. They thought that the umbrella clause

12 - RUDOLF DOLZER & MARGRETE STEVENS, BILATERAL INVESTMENT TREATIES 81-82 (1995)

has another function that I will explain in further details the coming chapters.

In this thesis, in the first chapter I will give a brief overview for the SGS cases as they were the first bullet in this war and mostly latter tribunals referred to one of the SGS cases. In the second chapter, I will analyse the wording usually used in umbrella clause drafting in BITS and whether the placement of the clause in the BIT has an indication in the interpretation process or not. In the Third chapter, I will discuss the four factors of every umbrella clause "function, scope, forum selection clause and privity" and how different tribunals and scholars dealt with those four factors. In the fourth chapter, I will discuss the future of the umbrella clause in BITs after all the disagreements and complications in the application process. Finally in the fifth chapter I will include my conclusions regarding all the problems discussed in this thesis.

Second chapter

"SGS cases"

The history of Arbitration is full of cases where tribunals had to interpret the umbrella clause, but It is obvious that the SGS cases against Philippines and Pakistan were the first bullet in this war. So it is reasonable to start by reading those awards carefully and find out how those tribunals dealt with the umbrella clause

A. SGS vs. Pakistan ¹³

On the 29th of September 1994 the government of Pakistan signed the PSI agreement with the claimant, whereby the claimant committed to provide “pre-shipment inspection” regarding certain goods from certain countries by a- SGS facilities and employees outside the host state and b- in the Pakistani ports with the help of the Pakistani customs.

The main purpose of this agreement was classifying the goods probably to determine the suitable tariff in order to increase the national income from the customs on the imported goods. The duration of the agreement was 5 years and the agreement was automatically renewable unless one of the parties refuses. Both parties had the right of termination the agreement after the first five years by a notice to the other party 3 months before the termination date. The agreement entered into force by the 1st of January 1995 and contained a dispute settlement provision in article 11 that stated " Any dispute, controversy or claim arising out of, or relating to this Agreement, or breach, termination or invalidity thereof, shall as far as it is possible, be settled amicably. Failing such amicable settlement, any such dispute shall be settled by arbitration in accordance with the Arbitration Act of the Territory as presently in force. The place of arbitration shall be Islamabad, Pakistan and the language to be used in the arbitration proceedings shall be the English language"

On 12 December 1996 the government of Pakistan notified the claimant that the agreement is terminated starting 11 March 1997.

The claimant initiated an ICSID arbitration against the host state alleging that "the Agreement was not “validly terminated” by the Respondent;13

13 - SGS Société Générale de Surveillance S.A. v. Islamic Republic of Pakistan, ICSID Case No. ARB/01/13

there was a “wrongful repudiation of contract” there was an “unlawful and ineffective” termination of the PSI agreement and there were “breaches of the PSI Agreement as well as violations of the BIT” that “therefore give rise to Pakistan’s liability to SGS for breach of contract, as well as its liability to SGS for infringement of the BIT”¹⁴

The BIT contained an umbrella clause in article 11 of the Swiss – Pakistan BIT 1995 that states :

"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."

The tribunal in this case chose to interpret the clause a restrictive interpretation where they did not refer to the rules of interpretation in VCLT articles 31&32 and they stated that "The text itself of Article 11 does not purport to state that breaches of contract alleged by an investor in relation to a contract it has concluded with a State (widely considered to be a matter of municipal rather than international law) are automatically “elevated” to the level of breaches of international treaty law”¹⁵

The tribunal presented four arguments to support their view

- a- Broad interpretation to the umbrella clause will lead to huge amounts of law cases in front of the international tribunals.
- b- Broad interpretation to the umbrella clause will make the other substantive protections of the BIT superfluous where they stated:
" the Claimant’s view of Article 11 tends to make Articles 3 to 7 of the BIT substantially superfluous”¹⁶
- c- The placement of the umbrella clause in the BIT is not among the substantive provisions of the BIT "articles 3-7"which support the tribunal point of view.
 - d – Broad interpretation to the umbrella clause will give the claimant the option of nullifying the "dispute settlement clause" in the agreement and

14 – Ibid para 17

15 Ibid para 166

16- Ibid para 168

make it pointless by giving the claimant the right to resort to international arbitration for any breach.

After reasoning their decision, the tribunal still had to explain the function of the umbrella clause if it was not promoting the contractual breaches into a treaty breach. They stated that the clause may promote the contractual breaches into a treaty breach in special circumstances such as: "State failure to participate in international arbitration with the investor after giving its consent or holding the investor from going to arbitration" This interpretation had its own share of Criticism especially not referring to the VCLT articles for interpretation. And the government of Switzerland took the unusual step by sending its disapproval over the interpretation reached by the tribunal in a letter to the Deputy Secretary-General of ICSID¹⁷.

b- *SGS vs. Philippines*¹⁸

During the late 1980s SGS made an agreement with the Philippines government. The purpose of this agreement was "pre-shipment inspection" for the goods exported to Philippines ports from certain states. SGS role was reporting the customs of Philippines the nature of the imported goods before shipping in order to determine the value of customs payable on such goods. On 1991 the "CISS" agreement was concluded between the two parties and SGS became responsible for pre-shipment inspection globally. The CISS included a dispute settlement mechanism in article 12 which state:

"The provisions of this Agreement shall be governed in all respects by and construed in accordance with the laws of the Philippines. All 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"¹⁹

17 - principles of international investment law , by R.Dozler and . Second edition p.171 footnote 317

18 - *SGS Société Générale de Surveillance S.A. v. Republic of the Philippines*, ICSID Case No. ARB/02/6

19 – article 12 of the CISS 1991

By April 1999 The BIT between Switzerland and Philippines came into force and a dispute settlement mechanism in article VIII which states "For the purpose of solving disputes with respect to investments Between a Contracting Party and an investor of the other Contracting Party and without prejudice to Article IX of this Agreement (Disputes between Contracting Parties, consultations will take place between the parties concerned.

2. If these consultations do not result in a solution within six months from the date of request for consultations, the investor may submit the dispute either to the national jurisdiction of the Contracting Party in whose territory the investment has been made or to international arbitration. In the latter event the investor has the choice between (a) the International Center for the Settlement of Investment Disputes.. (b) an ad hoc arbitral tribunal which unless otherwise agreed upon by the parties to the dispute shall be established under the arbitration rules of the United Nations Commission on

International Trade Law (UN.C.I.T.R.A.L.).4. The Contracting Party which is a party to the dispute shall not at any time during the procedures, assert as a defense its immunity or the fact that the investor has received compensation under an insurance contract covering the whole or part of the incurred damage or loss. 5. Neither Contracting Party shall pursue through diplomatic channels a dispute submitted to international arbitration unless the other Contracting Party does not abide by and comply with the award rendered by such an arbitral tribunal. 6. The arbitral award shall be final and binding for the parties involved in the dispute, and shall be executed according to national law." ²⁰

The BIT also had an umbrella clause in article X/2 that states:

"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"²¹

By 2000 a dispute had arose between the two parties of the CISS agreement²². SGS initiated ICSID arbitration against the host state for not paying invoices for around 200 million CHF. The claimant described the failure of the respondent to pay those invoices as: a- breach for the FET treatment in the Swiss- Philippines BIT. b- Expropriation .c- breach to the umbrella clause. And the claimant stated that the tribunal has jurisdiction to look into the merit of the dispute by the consent giving by the respondent in article VIII in the BIT.

Philippines objected the jurisdiction of the tribunal for several reasons: a- The existence of a forum selection clause in the agreement between the parties. b- According to the BIT, SGS did not have an investment in the territory of Philippines. C- The dispute is a contractual dispute in its nature and cannot be treated as a treaty dispute. D- If the tribunal reached the conclusion that they have jurisdiction, that jurisdiction only covers the duration after the BIT becomes in force.

The tribunal concluded that SGS had an investment in Philippines according to the definition of the investment in article I/2 of the BIT²³. the tribunal also decided that the umbrella clause "means what it says"²⁴ and that tribunal has the jurisdiction to look into the contractual breaches according to the governing law for the agreement not the international law and that the existence of a dispute settlement mechanism in the agreement does not conflict referring commercial breaches to the international arbitration. They also decided that the dispute settlement mechanism in the BIT cannot override the "forum selection clause" in the agreement²⁵. As a result for all the mentioned above, the tribunal decided that they have limited jurisdiction to look in to the merit of the dispute but such claims were inadmissible because of the existence of the forum selection clause

21 – article X/2 of Swiss – Philippines BIT 1999

22 - Comprehensive Import Supervision Service Agreement, August 23, 1991.

23 - SGS v. Philippines, ICSID Case No. ARB/02/6 para 165 - 168

24 – Ibid . para 119

25 – Ibid . Para 96

in the agreement between the parties so the tribunal subsequently stayed the proceedings.

Professor Crivellaro dissented the opinion of the two other arbitrators and declared that he thinks that the ICSID tribunal should determine the merit of the dispute and do not stay the proceedings.²⁶

The tribunal chose to interpret the umbrella clause a broad interpretation by enabling the clause to promote the contractual breaches into a treaty breach, but unfortunately they did not carry this approach to its logical conclusion by looking into the merit of the dispute instead, they decided to stay the proceedings.

26- Contractual Claims and Bilateral Investment Treaties ,by Judith Gill; Matthew Gearing; Gemma Birt p. 399-401

Third chapter

Wording and placement of the umbrella clause in the BIT

In order to understand why umbrella clause is such Controversial topic, we need to analyse every aspect. And one of the most important aspects is the wording used to draft the clause and the placement of the clause in the BIT.

1 –Wording of the umbrella clause :

By looking at many models of umbrella clauses in different BITs, it seems that a certain wording in the BIT might have future influence when international tribunals interpret the clause to settle future disputes. Some would say that all umbrella clauses are alike but actually they are not²⁷. At the beginning and as a common factor there is the mandatory wording of the clause and it is worth noting that certain degree of mandatory is used when drafting the clause:

A- The most severe mandatory wording, and it can be found in terms like "shall observe" or "shall respect" and we can find this wording in Article 8(2) of the German Model BIT 1991(2) reads:

“Each Contracting Party shall observe any obligation it has assumed with regard to investments in its territory by nationals or companies of the other Contracting Party”

B- a less severe mandatory wording can be found In article 10 of the Australia-Poland BIT which states :

“A Contracting Party shall subject to its law do all in its power to ensure that a written undertaking given by a competent authority to a national of the other Contracting Party with regard to investment is respected”

Also most of the scholars consider that the famous umbrella clause in the Swiss – Pakistan BIT 1995 in article 11 is categorized among the second type "Less severe mandatory wording"²⁸

27 - professor Kaj Hober during module two seminars 2018-2019

28- The impact of investment treaties on contracts between host states and foreign investors by, Jan Ole Voss p.231

Looking into the different wordings for the umbrella clauses in different BITS, we can find that also the wording for the scope of the clause is different

A – Some umbrella clause drafters use the words "commitments" or "any obligation" to declare the scope of the clause and the interpretation of those words covers the contractual obligations and the unilateral obligations and we can find this wording in article 8(2) of the German Model BIT 1991(2) reads:

"Each Contracting Party shall observe any obligation it has assumed with regard to investments in its territory by nationals or companies of the other Contracting Party"

B – The other pattern of the clauses drafting usually has a more certain wording regarding the scope of the clause using words such "written" as in article 11 of China – Australia BIT 1988 which states :

"A Contracting Party shall, subject to its law, adhere to any written undertakings given by a competent authority to a national of the other Contracting Party with regard to an investment in accordance with its law and the provisions of this Agreement"

And other drafters use "contractual obligations" precisely as we can find in the Austria – Chile BIT 1997 in article 2/4 which state

"Each Contracting Party shall observe any contractual obligation it may have entered into towards an investor of the other Contracting Party with regard to investments approved by it in its territory "²⁹(Jan Ole Voss 2011)

2- The placement of the umbrella clause in the BIT:

The place of the umbrella clause in the BIT became an important factor since the tribunal in SGS vs. Pakistan used it as an indication to the parties intentions and that the placement of the clause in the BIT was one of the reasons why the tribunal chose the restrictive interpretation for the umbrella clause as they stated:

29 - The impact of investment treaties on contracts between host states and foreign investors by, Jan Ole Voss p.232

"Another consideration that appears to us to support our reading of Article 11 of the BIT, is the location of Article 11 in the BIT. The context of Article 11 includes the structure and content of the rest of the Treaty. We note that Article 11 is not placed together with the substantive obligations undertaken by the Contracting Parties in Articles 3 to 7"³⁰ .

In general there are three patterns where the umbrella clause is placed in the BIT:

a- Among the substantive provisions and usually this placement leads to the broad interpretation to the umbrella clause as this placement for the umbrella clause among the substantive provisions indicates to the intention of the parties to treat it as a substantive provisions and this placement can be found in the Netherlands, United kingdom, Japan and Sweden Model BITs.

b- Placement of the clause in the part addressed "Other commitments" in the BIT and this part usually is at the end of the BIT after the substantive provisions and the dispute resolution clauses. This placement is usually found in the Swiss, Finnish and Greek Model BITs.

c- Placement of the clause in a separate part from the substantive provisions and before the dispute resolution clauses. This placement is usually found in the German Model BITs³¹

30 – Ibid para 169

31 - Yannaca-Small, K. (2006), "Interpretation of the Umbrella Clause in Investment Agreements", OECD Working Papers on International Investment, 2006/03, OECD Publishing p.9&10

Forth Chapter
Interpretation of the Umbrella Clause
"Function, Scope, Forum selection clause and privity"

Different tribunals interpreted umbrella clauses differently. The main factors for every umbrella clause when they were interpreted are "Function, Scope, Forum selection clause and privity" and in this chapter I will discuss every factor of the four, showing how different tribunals dealt with it, trying to reach a conclusion on how umbrella clause will be interpreted in the future by international tribunals.

a- Function

What I mean in this thesis by the term "function" is the purpose of the clause. In different words, the reason why the parties included this certain clause in the BIT and the effect desired by them. By reviewing some of the available English Awards that considered umbrella clause, we could find four different patterns for the tribunal interpretation for the function of the clause.

1- A slogan.

In this pattern the tribunals dealt with the clause as a "slogan" and never give it actual function. They believe that the clause was put in the treaty just to encourage the host state to treat the investor fairly and to ensure the investor that he will be treated fairly but without any factual consequences in case of breaching the clause.

As an example for the tribunals who followed this pattern, the tribunal of *SGS vs. Pakistan* where the tribunal did not give any affect for the clause on the breaches alleged by the claimant, but it is also worth noting that they stated that it might have a function in special circumstances:

" we do not preclude the possibility that under exceptional circumstances, a violation of certain provisions of a State contract with an investor of another State might constitute violation of a treaty provision (like Article 11 of the BIT) enjoining a Contracting Party

constantly to guarantee the observance of contracts with investors of another Contracting Party"³²

We can also find this pattern in *Salini vs. Jordan*³³. In this case the tribunal also did not provide any function for the umbrella clause in article 2(4) of Italy – Jordan BIT and they stated:

" under Article 2(4), each Contracting Party did not commit itself to 'observe' any 'obligation' it had previously assumed with regard to specific investments of investors of the other contracting Party as did the Philippines. It did not even guarantee the observance of commitments it had entered into with respect to die investments of the investors of the other Contracting Parties as did Pakistan. It only committed itself to create and maintain a legal framework apt to guarantee the compliance of all undertakings assumed with regard to each specific investor"³⁴

2 – Umbrella clause and sovereign power

Umbrella clauses are only affective against sovereign power breaches. In this pattern the tribunals only gave affect to the clause whenever the host state breach is associated with sovereign powers. We can find an example for this pattern in many cases such "*Joy mining vs. Egypt*"³⁵

Where the tribunal stated:

"The Tribunal concludes therefore that, even if for the sake of argument there was an investment in this case, the absence of a Treaty-based claim, and the evidence that, on the contrary, all claims are contractual, justifies the finding that the Tribunal lacks jurisdiction. Neither has it been credibly alleged that there was Egyptian State interference with the Company's contract rights"³⁶
The tribunal in this case decided that they do not have jurisdiction to decide the case because they found that the claimant did not have an

32- Ibid para 172

33- *Salini Costruttori S.p.A. and Italstrade S.p.A. v. The Hashemite Kingdom of Jordan*, ICSID Case No. ARB/02/13

34 – Ibid para 126

35 - *Joy Mining Machinery Limited v. Arab Republic of Egypt*, ICSID Case No. ARB/03/11

36 – Ibid para 82

investment in Egypt yet, they went on and explained their point of view for the function of the umbrella clause which is in their opinion is activated by the existence of sovereign powers.

The same pattern is noted in other cases such: *El paso vs. Argentina*³⁷ , *Pan American v. Argentina*³⁸ and *Malicorp v. Egypt*³⁹

3 – Transform domestic obligations into international obligations.

The third pattern for the tribunals is that the function of the umbrella clause is to convert or transform the nature of the domestic obligations into international obligations. This means that they think that the clause is a tool that is used to change the nature of the obligations.

We can find this pattern in cases such "*Noble v. Romania*"⁴⁰ where the tribunal stated:

"An umbrella clause is usually seen as transforming municipal law obligations into obligations directly cognizable in international law"⁴¹and also added "two States may include in a bilateral investment treaty a provision to the effect that, in the interest of achieving the objects and goals of the treaty, the host State may incur international responsibility by reason of a breach of its contractual obligations towards the private investor of the other Party, the breach of contract being thus "internationalized", i.e. assimilated to a breach of the treaty. In such a case, an international tribunal will be bound to seek to give useful effect to the provision that the parties have adopted"⁴²

We can find the pattern in cases such: *Siemens v. Argentine*⁴³.

37 - *El Paso Energy International Company v. The Argentine Republic*, ICSID Case No. ARB/03/15

38 - *Pan American Energy LLC and BP Argentina Exploration Company v. The Argentine Republic*, ICSID Case No. ARB/03/13

39 - *Malicorp Limited v. The Arab Republic of Egypt*, ICSID Case No. ARB/08/18

40 - *Noble Ventures, Inc. v. Romania*, ICSID Case No. ARB/01/11

41 – *Ibid* para 53

42 – *Ibid* para 54

43 - *Siemens A.G. v. The Argentine Republic*, ICSID Case No. ARB/02/8

4- Jurisdiction Tool

The Forth pattern that we can find is that, the function of the clause is not changing the nature of the obligations, or changing the applied law or changing the scope of the obligations, but it is only a tool that gives international tribunal jurisdiction to look into disputes that would not have jurisdiction to look into in normal circumstances.

We can find this pattern in *SGS vs. Philippine*⁴⁴ where the tribunal stated: " this is not what Article X(2) of the Swiss-Philippines Treaty says. It does not convert non-binding domestic blandishments into binding international obligations. It does not convert questions of contract law into questions of treaty law. In particular it does not change the proper law of the CISS Agreement from the law of the Philippines to international law. Article X(2) addresses not the scope of the commitments entered into with regard to specific investments"⁴⁵ the same pattern is also found in the annulment committee decision in *CMS vs. Argentina* as the committee stated " The effect of the umbrella clause is not to transform the obligation which is relied on into something else; the content of the obligation is unaffected, as is its proper law"⁴⁶

The same pattern can be found in other cases such: *Limier v. Ukraine*⁴⁷ and *Burlington v. Ecuador*⁴⁸

b- Scope

The scope in this thesis is the nature of the obligations that the umbrella clause working on. And by reviewing investments awards we could find three patterns; a- the contractual obligations only, b- the contractual obligations without discussing the other kinds of obligations-unilateral- c- any obligations. I will discuss those three patterns with some details showing examples of investment awards.

44 - *SGS Société Générale de Surveillance S.A. v. Republic of the Philippines*, ICSID Case No. ARB/02/6

45 – *Ibid* para 126

46 annulment committee decision *CMS vs. Argentina* para 95lc

47 - *Joseph Charles Lemire v. Ukraine*, ICSID Case No. ARB/06/18

48 - *Burlington Resources Inc. v. Republic of Ecuador*, ICSID Case No. ARB/08/5

1 – Only the contractual obligations.

In this pattern the tribunal chose to operate the umbrella clause only on the contractual obligations, where there is a consensual agreement. This means that they excluded the unilateral obligations out of the scope of the umbrella clause.

We can find this pattern in the decision of the annulment committee in CMS vs. Argentina⁴⁹ where they stated:

"(a) In speaking of "any obligations it may have entered into with regard to investments", it seems clear that Article II(2)(c) is concerned with consensual obligations arising independently of the BIT itself (i.e. under the law of the host State or possibly under international law). Further they must be specific obligations concerning the investment. They do not cover general requirements imposed by the law of the host State.

(b) Consensual obligations are not entered into erga omnes but with regard to particular persons. Similarly the performance of such obligations or requirements occurs with regard to, and as between, obligor and obligee."⁵⁰

And the same position was taken by the tribunal of "Nobel vs. Romania"⁵¹ where they stated:

"In fact, one may ask what other obligations can the parties have had in mind as having been "entered into" by a host State with regard to an investment. The employment of the notion "entered into" indicates that specific commitments are referred to and not general commitments, for example by way of legislative acts. This is also the reason why Art. II (2)(c) would be very much an empty base unless understood as referring to contracts."⁵²

Both tribunals declared clearly that the umbrella clause scope is the contractual obligations only in their awards.

49 - annulment committee decision CMS vs. Argentina

50 – ibid para 95 / a&b

51 – Noble Ventures, Inc. v. Romania, ICSID Case No. ARB/01/11

52 – ibid para 51

2 – The scope of the clause covers the contractual obligations without an indication to the other kind of obligations.

As it is mentioned in the subtitle in those cases the tribunals confirmed that the scope of the clause covers the contractual obligations but they did not have to discuss the effect of the umbrella clause on the other kinds of obligations " unilateral obligations" as those obligations were not before the tribunal during looking into those disputes.

We can find this pattern in many cases such: SGS vs. Philippines⁵³ where the tribunal state:

" The term "any obligation" is capable of applying to obligations arising under national law, eg. those arising from a contract; indeed, it would normally be under its own law that a host State would assume obligations"⁵⁴ and we can also find the same pattern in MTD vs. Chile⁵⁵ as the stated " The Tribunal notes the statement of the Respondent that under international law the breach of a contractual obligation is not ipso facto a breach of a treaty. Under the BIT, by way of the MFN clause, this is what the parties had agreed. The Tribunal has to apply the BIT. The breach of the BIT is governed by international law. However, to establish the facts of the breach, it will be necessary to consider the contractual obligations undertaken by the Respondent and the Claimants and what their scope was under Chilean law"⁵⁶

3 – The scope of the clause covers "any obligation"

In this pattern the tribunals declared that the scope of the clause cover all kinds of obligations "contractual obligations & unilateral obligations" and not limited to contractual obligations.

53 - SGS Société Générale de Surveillance S.A. v. Republic of the Philippines, ICSID Case No. ARB/02/6

54 –ibid para 115

55 - MTD Equity Sdn. Bhd. and MTD Chile S.A. v. Republic of Chile, ICSID Case No. ARB/01/7

56 – ibid para 187

We can find this pattern in cases such: LG&E vs. Argentine⁵⁷ where the tribunal stated:

"As such, Argentina's abrogation of the guarantees under the statutory framework – calculation of the tariffs in dollars before conversion to pesos, semi-annual tariff adjustments by the PPI and no price controls without indemnification – violated its obligations to Claimants' investments. Argentina made these specific obligations to foreign investors, such as LG&E, by enacting the Gas Law and other regulations, and then advertising these guarantees in the Offering Memorandum to induce the entry of foreign capital to fund the privatization program in its public service sector. These laws and regulations became obligations within the meaning of Article II(2)(c), by virtue of targeting foreign investors and applying specifically to their investments, that gave rise to liability under the umbrella clause."⁵⁸

The same pattern can be found in Enron vs. Argentina⁵⁹ where the tribunal stated:

"Under its ordinary meaning the phrase 'any obligation' refers to obligations regardless of their nature. Tribunals interpreting this expression have found it to cover both contractual obligations such as payment as well as obligations assumed through law or regulation"⁶⁰

C – Forum selection clause

This part is dedicated to the case where tribunals are looking at contractual breaches and at the same time they are faced with a "forum selection clause" in the contract between the parties. In that case the tribunal has to balance between their interpretation for the umbrella clause and their jurisdiction to look into the merits of the dispute with the forum selection clause in the contract. By looking at different awards from

57 - LG&E Energy Corp., LG&E Capital Corp., and LG&E International, Inc .v. Argentine Republic, ICSID Case No. ARB/02/1

58 – ibid para 175

59 - Enron Corporation and Ponderosa Assets, L.P. v. Argentine Republic, ICSID Case No. ARB/01/3

60 – ibid para 274

different tribunals I could spot three positions for the tribunals: 1-the tribunal decided they lack jurisdiction because of the existence of the "Forum selection clause" 2- the tribunal decided they have jurisdiction but they won't look into the merits, 3- the tribunal has jurisdiction regardless the "forum selection clause" and I am going to discuss those positions with further details.

1 – Lack of jurisdiction.

The tribunal in this approach decided that they do not have jurisdiction looking in to the merit of the dispute because of the existence of "forum selection clause"

This pattern can be found in *Toto vs. Lebanon*⁶¹ where the tribunal stated: "Although Article 9.2 of the Treaty may be used as a mechanism for the enforcement of claims, it does not elevate pure contractual claims into treaty claims. The contractual claims remain based upon the contract; they are governed by the law of the contract and may be affected by the other provisions of the contract. In the case at hand that implies that they remain subject to the contractual jurisdiction clause and have to be submitted exclusively to the Lebanese courts for settlement. Because of this jurisdiction clause in favor of Lebanese courts, the Tribunal has no jurisdiction over the contractual claims arising from the contract referring disputes to Lebanese courts"⁶²

The tribunal decision was based on the opinion that says; umbrella clause does not change the nature of the obligations and that they remain subject to the provisions of the contract. In general I did not spot this pattern in many cases.

2 - The tribunal decided they have jurisdiction but claims are inadmissible.

In this assumption the tribunal confirmed that umbrella clause gave them jurisdiction to look in to the dispute but, the existence of a "forum

61 - *Toto Costruzioni Generali S.p.A. v. The Republic of Lebanon*, ICSID Case No. ARB/07/12

62 – *ibid* Para 202

selection clause" precludes the tribunal to look into the merits of the dispute.

This pattern can be found in *BIVAC vs. Paraguay*⁶³ where the tribunal stated:

"For the reasons set out above, assuming that Article 3(4) of the BIT provides a basis for the exercise of jurisdiction by the tribunal over claims relating to the Contract, we conclude that the claim in relation to Article 3(4) is inadmissible, because:

- (1) In Article 9(1) of the Contract the parties agreed to a legally binding exclusive jurisdiction clause which provided for the resolution of "any conflict, controversy or claim which arises from or is produced in relation to [the] Contract" only by the Tribunals of the City of Asunción;
- (2) Article 3(4) of the BIT does not override the exclusive jurisdiction clause of Article 9(1) of the Contract;
- (3) "the fundamental basis of the claim" presented by BIVAC in respect of Article 3(4) of the BIT concerns a "conflict, controversy or claim" arising from or produced in relation to the Contract;
- (4) having regard to the need to respect the autonomy of the parties, BIVAC cannot rely on the Contract as the basis of a claim under Article 3(4) of the BIT when the Contract itself refers that claim exclusively to another forum, in the absence of exceptional reasons which might make the contractual forum unavailable;
- (5) the proper forum for the resolution of the contractual claim that has been raised under Article 3(4) of the BIT is the Tribunals of the City of Asunción, applying the law of Paraguay.

160. Having concluded that the claim under the umbrella clause is inadmissible, the normal course would be to dismiss the claim."⁶⁴

The same pattern can be found in *SGS vs. Philippines*.⁶⁵

63 - *BIVAC B.V. v. The Republic of Paraguay*, ICSID Case No. ARB/07/9

64 - *Ibid* Para 159&160

65 - *SGS Société Générale de Surveillance S.A. v. Republic of the Philippines*, ICSID Case No. ARB/02/6

3 – The tribunal has absolute jurisdiction regardless the forum selection clause:

In this approach the tribunals decided they have jurisdiction to look into the merits of the case regardless the existence of the forum selection clause. And the reason behind this approach that the contractual breach under the effect of the umbrella clause became a treaty breach and it is legally accepted that treaty breaches are not subject to the forum selection clause in the contract⁶⁶.

This pattern can be found in *SGS v. Paraguay*⁶⁷ where the tribunal stated: "Given that the Tribunal does not adopt Respondent's characterization of Claimant's claims as contractual rather than treaty claims, the Contract's forum selection clause is readily disposed of. That is, if Claimant had not advanced claims for breach of the Treaty and had brought forward only claims for breach of the Contract, we would be faced with different questions, including the relationship between Article 9 of the Contract (providing for dispute resolution of contract claims in the courts of the City of Asunción) and Article 9 of the BIT (providing for resolution of "disputes with respect to investments"). Here, however, we accept that Claimant has stated claims under the Treaty, and so the question before us is simply whether a contractual forum selection clause can divest this Tribunal of its jurisdiction to hear claims for breach of the Treaty. The answer to that question is undoubtedly negative.

139. On this point, both the Vivendi I tribunal and the Vivendi I annulment committee were in agreement. According to the tribunal, a forum selection clause of a contract "does not divest this Tribunal of jurisdiction to hear this case because that provision did not and could

66 - ("Vivendi" or "Vivendi Annulment"), Case No. ARB/97/3, Decision on Annulment of 3 July 2002, para 98

67 - *SGS Société Générale de Surveillance S.A. v. The Republic of Paraguay*, ICSID Case No. ARB/07/29

not constitute a waiver by [claimant] of its rights under Article 8 of the BIT to file the pending claims against the Argentine Republic."⁶⁸

D – The privity of the clause

The fourth factor that tribunals still have differences trying to interpret the umbrella clause is privity and by "privity" we mean the situation when there is a contractual breach and the investor or the respondent or both of them, are not parties to the contractual relationship.

For the investor side, the claimant may be "a share holder" who is not a party to the contract with the host state who initiated the arbitration against the host state. The tribunals did not treat this case "share holder" similarly. Some tribunals decided that claimant in this case cannot use the obligations of a contract that he is not a party to. Other tribunals decided that those obligations are close related to the investment of the claimant and accordingly subject to the protection of the umbrella clause and the claimant does not have to be a party to the contract.

For the host state side, the tribunals also have their differences. Some tribunals decided that the obligations of the state entities that enjoy independent legal personality cannot be attributed to the state. The other tribunals did not find a reason that prevents them attributing the state entities obligations to the state according to the international law rules⁶⁹. In the coming pages, I am going to discuss the privity issue in further details.

I – The investor

a- Privity is a must.

In this approach when the investor "claimant" is not a party to the contract the tribunals refused to give the claimant the right to initiate arbitration against the host state declaring that his investment is not subject to the protection of the umbrella clause. The main reason for the tribunals that

68 – Ibid para 138&139

69 - principles of international investment law , by R.Doizler and . Second edition p.175-177

require privity for applying the umbrella clause was that the claimant is not a party to the contract.

We can find this pattern in *Siemens vs. Argentina*⁷⁰ where the tribunal stated:

"The Tribunal considers that Article 7(2) has the meaning that its terms express, namely, that failure to meet obligations undertaken by one of the Treaty parties in respect to any particular investment is converted by this clause into a breach of the Treaty. Whether an arbitral tribunal is the tribunal which has jurisdiction to consider that breach or whether it should be considered by the tribunals of the host State of the investor is a matter that this Tribunal does not need to enter. The Claimant is not a party to the Contract and SITS is not a party to these proceedings.

205. In regards to the scope of Article 10(1), the Tribunal concurs with the submission that reference to disputes related to investments would cover contractual disputes for purposes of the consent of the parties to arbitration given the wide meaning of the term "investments" and the terms of Article 7(2). However, to the extent that the obligations assumed by the State party are of a contractual nature, such obligations must originate in a contract between the State party to the Treaty and the foreign investor as, for instance, in the *SGS cases*⁷¹

b – Privity is not a must

In this approach the claimant was not a party to the contract and yet the tribunal accepted the claims of the claimant and the main reasoning for those tribunals was that those contracts were related to the investment of the claimant which give the claimant the right to initiate arbitration against the host state even if the claimant is not a party to the contract.

We can find this pattern in *Continental Casualty vs. Argentina*⁷² where the tribunal stated:

70 - *Siemens A.G. v. The Argentine Republic*, ICSID Case No. ARB/02/8

71 – *Ibid* Para 204&205

72 - *Continental Casualty Company v. The Argentine Republic*, ICSID Case No. ARB/03/9

"The covered obligations must have been entered "with regard to" investments. Thus they must concern one or more investments and, moreover, must address them with some degree of specificity. They are not limited to obligations based on a contract. Finally, provided that these obligations have been entered "with regard" to investments, they may have been entered with persons or entities other than foreign investors themselves, so that an undertaking by the host State with a subsidiary such as CNA is not in principle excluded"⁷³

II – The host state

A - Privity is a must.

This approach was based on that as long as the entity enjoys its own legal personality apart from the government, the obligations of the entity cannot be attributed to the state according to the principle of "pacta tertiis nec nocent nec prosunt" ⁷⁴

This pattern can be seen in *Impregilo vs. Pakistan*⁷⁵ where the tribunal stated:

"In the Tribunal's view, given that the Contracts were concluded by Impregilo with WAPDA, and not with Pakistan. Impregilo's reliance upon Article 3 of the BIT takes the matter no further. Even assuming arguendo that Pakistan, through the MFN clause and the Swiss-Pakistan BIT, has guaranteed the observance of the contractual commitments into which it has entered together with Italian investors, such a guarantee would not cover the present Contracts – since these are agreements into which it has not entered. On the contrary, the Contracts were concluded by a separate and distinct entity."⁷⁶

B - Privity is not a must

This approach was basically based on the rules of attribution using the ILC's Articles on State Responsibility (ILC Articles) and whenever the

73 – Ibid Para 297

74 - Umbrella Clause and Privity of Contract By the author p. 5

75 - *Impregilo S.p.A. v. Islamic Republic of Pakistan*, ICSID Case No. ARB/03/3

76 – Ibid Para 223

tribunal find that entity breaches can be attributed to the state using the "ILC articles", they apply the umbrella clause even though the state is not a party to the contract."Mohamed Ahmed 2019"⁷⁷

This pattern can be found in *Eureko vs. Poland*⁷⁸ where the tribunal stated: " In the view of the Tribunal, there can be no doubt that the Minister of the State Treasury, in the present instance, when he sold to the Eureko Consortium 30% of the State Treasury's shareholding interest in PZU by virtue of the SPA and undertook in the First Addendum to carry out an IPQ as to an additional 21 % of the shareholding, or, under the Second Addendum, sell it outright to Eureko, was acting pursuant to clear authority conferred on him by decision of the Council of Ministers of the Government of Poland in conformity with the officially approved privatization policy of that Government. As such, the Minister of the State Treasury engaged the responsibility of the Republic of Poland. Moreover, the record before the Tribunal is spangled with decisions of the Council of Ministers in respect of the PZU privatization which authorize the State Treasury Minister or Ministry to take actions, some of which the Tribunal concludes later in its Award were in breach of Poland's obligations under the Treaty"⁷⁹

This was a revision for the main four factors that tribunals do not agree upon with case examples.⁸⁰

77 – privity of the umbrella clause by the author 2019

78 - *Eureko vs. Poland* , partial award 19 August 2005

79 – Ibid Para 129

80 - Umbrella Clauses Since *SGS v. Pakistan* and *SGS v. Philippines* - A Developing Consensus by JUDE ANTONY p. 613-634

Fifth chapter

Future of the umbrella clause

After demonstrating different analysis for the factors of the umbrella clause by different tribunals in the forth chapter, I think it is very hard to reach Jurisprudential consensus regarding the application of the umbrella clause. Tribunals reached different conclusions regarding the contractual and treaty obligations, if the breach combined with sovereign power or not, the application of the umbrella clause when the contract has a forum selection clause and privity of the contract.

The best example for the inconsistency regarding the application of the umbrella clause is the SGS cases, *SGS vs. Pakistan*⁸¹, *SGS vs. Philippines*⁸² and *SGS vs. Paraguay*⁸³. the BITs in those cases were semi identical and the claimant is the same in all cases. Also the contract was a pre shipment inspection contract in the three cases, yet the outcome of every case was different. While the tribunal of *SGS vs. Pakistan* adopted a restrictive interpretation to the umbrella clause, the *SGS vs. Philippines* took the opposite position and adopted a broad interpretation for the umbrella clause but decided to stay the proceedings. The tribunal of *SGS vs. Paraguay* adopted a broader interpretation. And since the three SGS cases, all the tribunals in investment cases containing umbrella clause choose to follow one of the SGS tribunals which can be best described by this charter⁸⁴ :

81 - *SGS Société Générale de Surveillance S.A. v. Islamic Republic of Pakistan*, ICSID Case No. ARB/01/13

82 - *SGS Société Générale de Surveillance S.A. v. Republic of the Philippines*, ICSID Case No. ARB/02/6

83- *SGS Société Générale de Surveillance S.A. v. The Republic of Paraguay*, ICSID Case No. ARB/07/29

84 - *Closing the umbrella: a dark future for umbrella clauses*. By, Raul Pereira de Souza Fleury

<i>SGS v. Pakistan</i>	<i>SGS v. Philippines</i>	<i>SGS v. Paraguay</i>
Interpretation	Interpretation	Interpretation
– <i>Toto v. Lebanon</i>	– <i>BIVAC v. Paraguay</i>	– <i>Eureko v. Poland</i>
– <i>Salini v. Jordan</i>	– <i>Bosh v. Ukraine</i>	– <i>Noble Ventures v. Romania</i>
– <i>El Paso v. Argentina</i>		– <i>Burlington v. Ecuador</i>
– <i>Siemens v. Argentina</i>		– <i>Duke Energy v. Ecuador</i>
– <i>Joy Mining v. Egypt</i>		

As a reasonable result for all the inconsistency, a change in the BIT drafting was a must. Some states fully excluded the umbrella clause out of their Model BITs such as: France, Canada, Colombia and India⁸⁵

Also the Norwegian Model BIT 2015 excluded the umbrella clause and the drafters stated regarding this issue :

"The point of departure for the work on a new model agreement has been that the Arbitration Tribunal shall only be able to consider alleged breaches of the standards in the interstate investment agreement. Therefore, no right is laid down in the model agreement for an investor to use the same arbitration tribunal to settle disputes arising out of a contractual relationship between an investor (or his investment) and the host country. The breach of agreement referred to in the model agreement as the subject for arbitration, and which thereby sets the mandate for the Arbitration Tribunal, must thus be a breach of the investment agreement."⁸⁶

Since December 2015 until 2017 "52" investment agreements were entered into by different states according to the United Nations Conference on

85 - Umbrella clauses: a trend towards its elimination. By Raul Pereira de Souza Fleury p.688

86- Comments on the Model for future Investment Agreements 29, 19 December 2007, <<http://www.italaw.com/sites/default/files/archive/ita1029.pdf>> p.29

Trade and Development (UNCTAD)⁸⁷ only 2 of those agreements contained umbrella clause, which is in my opinion a great indication to the future of the umbrella clause.

It is also worth noting that states as: Argentina, Paraguay, Philippines, Romania and Jordan who were affected severely by the umbrella clause or threatened by the Umbrella clause Refrained signing any investment agreements which include umbrella clause.⁸⁸

87 - Closing the umbrella: a dark future for umbrella clauses. By, Raul Pereira de Souza Fleury
88 – Ibid p. 690

Sixth Chapter

Conclusion

The main purpose for including umbrella clauses in BITs was always "to bring the contractual obligations under the same protection provided for the treaty obligations". Two different sets of obligations were put in one basket.

The differences between the two sets are great. First, while the source of the treaty obligations is the treaties organized by international law, the source of the contractual obligations is contract organized usually by the domestic law of the host state. Secondly, while the treaty breach results in international responsibility organized by the 2001 Draft Articles on Responsibility of States for Internationally Wrongful Acts, the contractual breach does not, unless the contractual breach is a treaty breach at the same time.

Trying to put two different sets of rules in one basket, resulted in Complexities. It is well known that the evolution of the international law regarding the rights and obligations of the states was quite hard and long until it reached the current stage. And most likely trying to push a set of new rules to the same legal frame may lead to the destruction of the whole legal frame. Also the procedures and formalities that every treaty goes through in every state are very strict and well organized because of the great responsibilities it may lead to, so it is not acceptable or reasonable that contractual obligations -usually concluded by an executive authority in the state- enjoy the same level of protection and may lead to state responsibility without going through all those formalities or procedures that treaty obligations go through.

For all the reasons above every tribunal dealt with the umbrella clause tried to offer their conclusion from their point of view. And those conclusions were different, which amounted in different interpretations and sometimes Contradictory for the same umbrella clause. Tribunals disagreed together over every factor. They disagreed over the function and the scope of the umbrella clause. Tribunals also went different ways regarding privity of the contract and how to deal with forum selection clauses in the contract.

For all those disagreements, it was expected that something will change. And it happened; states stopped including their BITs the umbrella clause. From December 2015 till 2017, "52" investment agreement were entered to by different states according to (UNCTAD) only 2 of those agreements contained umbrella clause which is under 4% and one of the two BITs which included umbrella clause was the Austria-Kyrgyzstan BIT 2016 and it stated in article 11:

"Each Contracting Party shall observe any obligation it may have entered into with regard to specific investments by investors of the other Contracting Party. This means, inter alia, that the breach of a contract between the investor and the host State will amount to a violation of this treaty"

It is clear that the two states worked on the wording of the umbrella clause in order to not be faced by the assumptions of the tribunals that may differ from their original intentions and maybe this the only way for the umbrella clause to survive in the investment world, better detailed wording.

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