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UMBRELLA CLAUSES WITHIN ENERGY CHARTER TREATY

Abstract

Since the late 1950s, international investment law has experienced a new term so-called 'umbrella clauses' aimed for the protection of the observance of obligations agreed between foreign investors and host states. However, since the beginning of the new milennium, the umbrella clauses have faced a bunch of criticism, being condemned on eradicating the difference between contracts and public international law. Wordings in international energy investment agreements, including Energy Charter Treaty have caused the question that whether these clauses cover all obligations or specific commitments to investors. In this article, the notion of umbrella clauses has been discussed and Article 10(1) of the Energy Charter Treaty has been explained by references to the case law of international arbitration courts.

Annotasiya

Ötən əsrin 50-ci illərinin sonlarından etibarən, beynəlxalq investisiya hüququnda xarici investorlar və ev sahibi dövlətlər arasında razılaşdırılan öhdəliklərin yerinə yetirilməsinə təminat məqsədi güdən və 'çətir müddəaları' adlanan yeni bir termin ortaya çıxmışdır. Buna baxmayaraq yeni minilliyin başlanğıcından bəri, çətir müddəaları müqavilə hüququ və beynəlxalq ümumi hüquq arasındakı fərqi ortadan qaldırması kimi bir sıra tənqidlərlə üz-üzə gəlmişdir. Beynəlxalq enerji investisiya sazişlərində, o cümlədən Enerji Xartiyası Sazişində istifadə olunan sözlər bu müddəaların bütün öhdəlikləri, yoxsa investorlar qarşısında qəbul edilən spesifik öhdəlikləri əhatə etməsi sualını doğurur. Bu məqalədə çətir müddəaları anlayışı müzakirə edilmiş, Enerji Xartiyası Sazişinin 10-cu maddəsinin 1-ci bəndi beynəlxalq arbitrajların presedent hüququna istinad olunmaqla izah edilmişdir.

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Introduction

Throughout the years, an increasing flow of investments from developed countries to developing ones has necessitated the conclusion of investment agreements between investors and invested states. When investors and host states reach a common point to finalize negotiations, they both usually sign investment contracts which are somewhere between treaties and private contracts.[1] In order to recover their market loss and avoid possible political risks, investors always look for contractual clauses which will at least relieve their damage. 'Umbrella clauses'[2] are one of these contractual clauses which are actively used by investors as a remedy for contractual breaches. They are quite prominent in the field of international investment law, as today two-fifths of more than 2700 BITs[3] contain umbrella clauses.[4] 'Umbrella clauses' has also an utmost importance in international investment law that Article 10(1) of the Energy Charter Treaty (ECT) comprises such a clause. In other words, foreign investors of state parties to the ECT can also bring their dispute before the treaty mechanisms and raise the question of state responsibility for contractual breaches.

This article is going to discuss the history and rationale of these clauses, in general, through the First Part. The Second Part will mainly focus on the ECT and the 'umbrella clause' contained therein. Although this article aims to discuss 'umbrella clauses' in relation to the ECT, it is not limited to the scope of the ECT, rather it overflows, from time to time, through the case law of the International Centre for Settlement of International Disputes (ICSID) and other dispute settlement institutions. However, the article will not touch *ratione personae* of the application of 'umbrella clauses' and will limit the scope with *ratione materiae*. All findings will be patched up in the Conclusion and final remarks will be introduced together with the author's views.

[1] E. Meurling & B. Volders, *Umbrella Clauses in International Investment Litigation*, 2 Eur. Procurement & Pub. Private Partnership L. R 80, 80 (2007).

[2] The clause is also referred as under the principle of *'pacta sunt servanda'* or the rule of *'sanctity of contract'* rule by some arbitration tribunals. *See, e.g., SGS Société Général de Surveillance S. A. v. The Islamic Republic of Pakistan*, , ICSID Case No. ARB/01/13, Decision of the Tribunal on Objections to Jurisdiction, ¶163 (6 August 2003), *see at:* https://www.italaw.com/cases/1009, (last visited: 26 October , 2017)

[3] Bilateral Investment Treaties.

[4] K. Yanacca-Small, Arbitration under International Investment Agreements: A Guide to the Key Issues, 483 (2010).

I. Origins and Rationale of Umbrella Clauses

A. Umbrella Clauses and Other Contractual Mechanisms

In any kind of investment relationships, an initial disequilibrium exists between a host state and an investor, mainly due to the unbalance between their bargaining powers. This stage is the outset of all transactions in an energy investment environment and the emergence of investment offers and acceptance, hence, especially foreign investors are dominant role players in energy investment negotiations with states. Grasping a strong bargaining power in their hands, foreign investors are mostly inclined to insert contract clauses that will provide a comprehensive protection[5] in favour of their investments. 'Umbrella clauses' stand out in this regard, as with their basic explanation, they enable foreign investors to elevate contractual claims up to the international level,[6] by a simple inclusion of the clause into BITs by their home state. Hence, the 'umbrella clauses' are different in character from other stabilization clauses because unlike other contractual clauses, the 'umbrella clause' is a product of negotiations between at least two states. Foreign investors do not include these clauses themselves, but these clauses enable them to sue host states relying on an article they did not even draft.

B. History and Origins of Umbrella Clauses

Historically speaking, the tendency of the inclusion of 'umbrella clauses' in International Investment Agreements (IIAs) originates from the tension between developed and developing countries.[7] The 'umbrella clauses' have started to appear in IIAs since the late 1950s as a part of the international investment movement, a kind of a reaction to the trend of liberal internationalism after the WWII and establishment of dispute settlement centres like the ICSID and Multilateral Investment Guarantee Agency (MIGA).[8] In 1959, the BIT concluded between Germany and Pakistan already contained the 'umbrella clause'.[9]

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[5] The comprehensiveness of the protection provided by the 'umbrella clauses' is reflected on the term itself, as BITs covers contractual obligations with its protective umbrella. C. Schreuer, *Travelling BIT Route: Of Waiting Periods, Umbrella Clauses and Forks in the Road*, 5 J. World Investment & Trade 232, 250 (2004).

[6] D.M. Zenginkuzucu, *Şemsiye Klozların ICSID Hakem Mahkemesinin Yargı Yetkisine Etkisi*, 1 Uluslararası Ticaret ve Tahkim Hukuku Dergisi 166, 173 (2013).

[7] J. Wong, *Umbrella Clauses in Bilateral Investment Treaties: Of Breaches of Contract, Treaty Violations, and Divide Between Developing and Developed Countries in Foreign Investment Disputes*, 14 Geo. Mason L. Rev. 137, 140 (2006).

[8] T.W. Wälde, *The Umbrella Clause in Investment Arbitration: A Comment on Original Intentions and Recent Cases*, 6 J. World Investment & Trade 184, 192 (2005).

[9] R. Dolzer & C. Schreuer, Principles of International Investment Law 167 (2012). E. Lauterpacht's legal advice to Anglo-Iranian Oil Company about the internationalization of contract obligations and further developments, such as Abs-Doelle Draft of 1958 and Article

The question why foreign investors need to include 'umbrella clauses' still in the presence of *'pacta sunt servanda'* principle may be of interest to this article. Wälde[10] found the answer in the notorious unwillingness of foreign investors' home states to invoke *'pacta sunt servanda'* principle for minor commercial disputes of their investors with host states, bearing in mind that the principle only covered interstate agreements.[11] When the properties of foreign investors in the host state were subject to a nationalization or expropriation, they became vulnerable, since they could not invoke international responsibility of host states, except the cases in which the due process of law of host states turned to be allegedly flawy. That hindrance was, to some extent, related to the concept of *'Calvo Doctrine'*.[12] This doctrine referred foreign investor-state agreements completely and exclusively to domestic law or in other words, the jurisdiction of host states.[13] In contrast, when 'umbrella clause' was developed as a new edition of *'pacta sunt servanda'*,[14] it was aimed to enable not only contracting parties but also the foreign investors to enforce IIAs for their investment disputes.[15]

From the author's perspective of, irrespective of the fact that *'pacta sunt servanda'* has not lost its international law character at all, they should not be considered tantamount to the 'umbrella clauses', because the latter is more specific for international investment law. But of course, the gist of our research lies in the historical evolution of the *'pacta sunt servanda'*, thereby its influence in this regard must be borne in mind.

2 of Abs-Shawcross Convention of 1959 were noteworthy milestones of the historical background of these clauses.

[10] Wälde, *supra note* 7, 192-3.

[11] For a thorough compilation and evaluation of doctrinal views on the applicability of the principle of *'pacta sunt servanda'* on energy investment contracts concluded between foreign investors and host states, *see also*, Mustafa Erkan, International Energy Investment Law: Stability Through Contractual Clauses, 160-6 (2011).

[12] Being classified as a body of international rule about jurisdictional matters on aliens in a foreign country and the restrictive scope of protection provided by their home state, this doctrine was advanced by Argentine diplomat Carlos Calvo in 1868 and restated by Argentine foreign minister Luis Maria Drago in 1902. For a more detailed explanation of 'Calvo Doctrine', *see*, Calvo Doctrine, https://www.britannica.com/topic/Calvo-Doctrine, (last visited: 29 October, 2017). In addition, one reflection of the philosophy behind the 'Calve doctrine' can be found in Article 27 of the ICSID Convention which prohibits the right of Contracting States on diplomatic protection.

[13] Wälde, *supra note* 7, 201.

[14] B.Ş. Köşgeroğlu, Enerji Yatırım Sözleşmeleri ve Bunların Uluslararası Yatırım Anlaşmaları ile Korunması 303 (2012).

[15] However, current practice reveals that states are reluctant to invoke this clause in favour of their investors' investment disputes, as the cases brought in front of miscellaneous dispute resolution centres are disputed, as a principle, by foreign investors.

C. The Link between Contractual and International Obligations

The logic behind the 'umbrella clause' explains that any investor who alleges the breach of the investment contract is able to invoke the concluded IIA and head to the international forum.[16] However, this situation is quite exceptional that in general, breaches of private contractual obligations end up with the hearing of cases before domestic courts or arbitration tribunals so agreed in investment contracts,[17] not at international arbitration facilities prescribed in IIAs. The main difference between contractual and treaty claims lies in the source of the right entitled.[18] It means that contractual claims only stems from private contracts, whereas treaty claims are always based on international treaties. Nevertheless, 'umbrella clauses' somehow fills the gap between contractual and international obligations. But is a single clause containing an observation of contractual obligations sufficient for holding contracting states of BITs or Multilateral Investment Treaties (MITs) responsible for the breach of the treaty? At this point, two clashing decisions issued independently by two arbitration tribunals respond to our question with "yes" and "no" in *SGS v. The Philippines*[19] and *SGS v. Pakistan cases* respectively that will be spoken of within the next part.

Switching the gears to the perspective of public international law, one can easily encounter with a strong critical opinion stating that state responsibility, as a part of treaties, is only a matter of public international law and it can only be invoked by contracting state parties to the agreements.[20] Hence, it should not be blended with results of contractual violations.[21] This argument was

[16] This case is still relevant even if the original contract with the host state has no provision for the settlement of disputes. *See*, José E. Alvarez, The Public International Law Regime Governing International Investment, 33 (2011). For a view explaining a notion of 'umbrella clauses" as an elevator of private contractual claims up to bilateral investment treaty breaches, and at the same time, entitling the parties to recourse to the dispute resolution mechanisms enumerated in bilateral investment treaties, *see also*, Dikran M. Zenginkuzucu, Uluslararası Ticaret ve Yatırım Uyuşmazlıklarında Dostane Çözüm: Kurumlar, Kurallar, Süreçler 9-10 (2013).

[17] Meurling & Volders, *supra note* 1, 81.

[18] Pedro Martini, *Umbrella Clauses in Investment Treaties*, 27 The International Litigation Quarterly 19, 19 (2011).

[19] *SGS Société Général de Surveillance S.A. v. The Philippines*, ICSID Case No. ARB/02/6, Decision of the Tribunal on Objections to Jurisdiction (29 January, 2004), *see at:* https://www.italaw.com/cases/documents/1019 (last visited 29 October, 2017).

[20] The Tribunal in the case of *SGS v. The Philippines* also touched this general principle, but eventually ignored it stating that this principle cannot be taken as an absolute principle, and it can only be referred as a method of interpretation. J. Bandrés de Lucas, *Umbrella Clause: Uncertain Contract Protection under IIAs*, 10 Revista de Globalización, Competitividad & Gobernabilidad 100, 107 (2016).

[21] Jaemin Lee, *Putting a Square Peg into a Round Hole? Assessment of the 'Umbrella Clause' from the Perspective of Public International Law*, 14 Chinese J. Int'l L. 341, 345-6 (2015).

further reinforced by the objectives of IIAs, most preambles of which aim to *"[s]trike a balance*[22] *between the interest of a foreign investor and the government of a host state."*[23] (emphasis added) However, this view, from the point of the author, can be contested by referring to the objective of international investment law, which is to protect foreign investors. That's why, in short, it always matters: whom do the parties intend to protect most?

In this respect, both extensive and restrictive interpretations of this clause will be analyzed together with their advantages and disadvantages but firstly, we find it appropriate to put a spotlight on Article 10(1) of Energy Charter Treaty.

II. Legal Nature of Umbrella Clauses and Energy Charter Treaty

A. An Overview of Energy Charter Treaty

In early 1990s, a bipartite need from Russia and its neighbouring countries, to be invested on the one side, and from Western block countries to export a capital and decrease the investment dependence on certain countries on the other side, were two sparking elements of the development of a uniform regional treaty for energy cooperation and investments.[24] With a global aim of building an integrated energy market by bridging Russian and Eastern European energy sector with Europe and the world, the ECT[25] is considered a constitution of international energy investment law.[26] Despite the ECT was

[22] Despite the fact that neither the Energy Charter Treaty, nor the ICSID Convention provides a plain provision for an objective of protecting the balance between parties, the provisions maintain that balance between the interests of an investor and the government of a host state in the ICSID Convention. *See*, Report of the Executive Directors of the International Bank for Reconstruction and Development on the Convention on the Settlement of Investment Disputes between States and Nationals of Other States, Chapter III, Article 13, 41, available at https://icsid.worldbank.org/en/Documents/icsiddocs/ICSID%20Convention%20English.pdf, (last visited: 7 November, 2017); Another reference to the balance and mutuality between benefits was given in *SGS v. Pakistan case*, *see*, *supra note* 2, para. 168.

[23] Lee, *supra note* 20, 350-351.

[24] Kaj Hober, *The Energy Charter Treaty: An Overview*, 8 J. World Investment & Trade 323, 324 (2007).

[25] Main objectives of the ECT are listed as development of trade in energy, cooperation in energy field and energy efficiency, environmental cooperation and dispute resolution. For more details of the ECT and the full text, *see*, The Energy Charter Treaty (With Incorporated Trade Amendment) and Related Documents, http://www.europarl.europa.eu/meetdocs/2014_2019/documents/itre/dv/energy_charter_/energy_charter_en.pdf (last visited: 30 October, 2017).

[26] The ECT entered into force on April 16, 1998, with 54 contracting parties and 39 countries with an observer status. Apart from the member countries who hold the observer status as well, 15 signatories of the EEC (1991) and 24 signatories of International Energy Charter (2015) are further accounted the observers of the Energy Charter Conference. For more information,

drafted for the implementation around the European region, the treaty has gradually evolved into a universal agreement after the accession of other countries from American and Asian continents.[27]

Concerning foreign investments, the ECT provides a regime *"[t]o establish level playing field for investments in the energy sector and to minimize non-commercial risks associated with such investments."*[28] (emphasis added) This MIT[29] also furnishes parties to any dispute with a right to resort to arbitration tribunals for dispute settlement provided that the party shall wait for minimum three months after the submission of the notice to the other.[30] Further, the ECT is one of those fewer agreements which contains an 'umbrella clause.' Although the ECT cannot be called a pure investment treaty because its scope is much more complex, obviously, the contracting parties have agreed even on the inclusion the 'umbrella clause.'

B. Evaluation Of Article 10(1) Of Energy Charter Treaty

1. Wording: Is The Content of the Umbrella Clause Necessary?

With regard to the protection, promotion and treatment of investments, Article 10(1) is of paramount importance. The last sentence of the Article 10(1) of the ECT reads as follows:

> "[E]ach Contracting Party shall observe any obligations it has entered into with an investor or an investment of an investor of any other Contracting Party."[31](emphasis added)

As will be discussed below, the wording in IIAs is the main point for the implementation of the clauses in investment contracts. While some IIAs use the language so that to be applied to any obligations, other investment treaties seem to keep the circumference of the umbrella quite specific. In this regard, although the wording of the ECT *prima facie* covers all obligations of contracting parties, the determinative expression of *"entered into"* restricts its

see also, Constituency of the Energy Charter Conference, http://www.energycharter.org/who-we-are/members-observers/ (last visited: 30 October, 2017).

[27] Ə. İ. Sadıqov, Beynəlxalq Enerji Hüququ 158 (2013).

[28] Hober, *supra note* 23, 325.

[29] To some extent, this treaty is not accounted as a "pure" investment treaty in the legal doctrine, because it also includes other issues, such as trade in goods and further economic and environmental activities. *See also*, Richard Happ, *Dispute Settlement under the Energy Charter Treaty*, 45 German Y.B. Int'l L. 331, 335 (2002).

[30] To compare, the ECT contains right to resort to diplomatic tools for environmental and power engineering disputes, instead of arbitration mechanisms, *see*, Sadıqov, *supra note* 26, 293.

[31] One explanation of this Article was made in the doctrine that no government is entitled to repeal an investment agreement or force an investor to renegotiate by using its sovereign powers. A. Konoplyanik & T. Wälde, *Energy Charter Treaty and Its Role in International Energy*, 24 J. Energy & Nat. Resources L.523, 535 (2006).

subject matter with contractual obligations.[32] However, it should not be denied that this provision protects foreign investors against political risks, in particular, governmental breaches of investment contracts which can either occur in legislative or administrative interventions.[33] The author does not notice any problem regarding such unfair measures, because Article 10 provides different standards of treatment for the investors of the contracting parties, any breach of which will, to a large extent, enable the investors to invoke the treaty protection.

Here the question arises if the words *"any obligations"* cover states' commercial obligations in front of foreign investors as well as governmental breaches. In *Eureko B.V. v. Poland case* as described above, the Tribunal dealt with the case rather pragmatically and emphasized the perceptibility of the 'umbrella clause' contained in the BIT concluded between the Netherlands and Poland by explaining the plain wording of the provision.[34] Most of the wordings of 'umbrella clauses' would be interpreted extensively if the interpretation was limited to the ordinary meaning of texts. But sometimes wording of 'umbrella clauses' *per se* can support restrictive interpretation as it did in the case of *Salini v. Jordan*.[35] Although, the author supports to broaden the horizon of interpretation instruments and go beyond the simple wording.

In addition to this question, the types of breach to be elevated to the international responsibility of states and the scope of Article 10(1) of the ECT in this respect will be analyzed in next sub-paragraphs.

2. Ratione Materiae: Governmental Breaches or Commercial Disputes?

At the first sight, it seems quite unreasonable to hold contracting parties of the ECT responsible for each commercial breach of investment disputes occurred in their territories. However, this debate is going even further and reaching the threshold of holding state parties responsible also for unilateral obligations and commitments under the protective umbrella of the IIAs. This

[32] *The Energy Charter Treaty: A Reader's Guide*, 26, available at https://is.muni.cz/el/1422/jaro2016/MVV2368K/um/ECT_Guide_ENG.pdf (last visited: 6 November 2017); For the same ground, *see also*, *Plama Consortium Limited v. The Republic of Bulgaria*, ICSID Case No. ARB/03/24, Award, ¶187 (27 August 2008), *see at:* https://www.italaw.com/cases/857

[33] Happ, *supra note* 28, 345.

[34] *Eureko B.V. v. The Republic of Poland*, ICSID, Decision of Partial Award, ¶246 (19 August 2005), see at: https://www.italaw.com/cases/412, accessed on October 30, 2017.

[35] The expressions *"[c]reate and maintain a legal framework apt to guarantee the compliance of undertakings"* (emphasis added) led to the dismissal of the Salini's argument by the Tribunal who stated that Jordan did not undertake anything with regard to the observation of undertakings, but only to create a legal framework. *See, Salini Construttori S.p.A. v. The Hashemite Kingdom of Jordan*,, ICSID Case No. ARB/02/13, Decision on Jurisdiction, ¶126 (9 November 2004), see at: https://www.italaw.com/cases/954, (last visited: 6 November 2017).

sub-paragraph will, without being limited to the wording of the Article 10(1) of the ECT, connote the restrictive and extensive interpretations of this clause.

2.1. Restrictive Approach

This approach is reasoned by referring to the fact that 'umbrella clauses', being a ground for derogation from one of the main principles of customary international law, should not be interpreted extensively.[36]

Two tendencies with regard to the restrictive legal nature of 'umbrella clauses' must be distinguished. The first tendency explains the 'umbrella clauses' without touching their function of bringing domestic claims before the international arbitration that is recognized by IIAs concluded between home and host states. This narrow approach was followed by doctrinal views[37] and a couple of arbitration awards[38]. In *SGS v. Pakistan case*, in order to interpret the BIT between Switzerland and Pakistan extensively, the Tribunal asked the claimant for *"[c]lear and convincing evidence…that such was indeed the shared intent of Contracting Parties…"*[39] (emphasis added), however, failed to get any of them at the end of the day. In *Joy Mining case*, the Tribunal reiterated that the 'umbrella clause' was ill-placed and refused the extensive implementation as previously it did in *SGS v. Pakistan case*.[40]

On the other hand, the second tendency within the narrow approach to the *ratione materiae* of 'umbrella clauses' exempts governmental breaches from all contractual violations and only, in this case, recognizes the attribution of treaty breaches to contractual violations under the shelter of 'umbrella clauses'.[41] This view was reflected in *El Paso case*[42], in which the Tribunal, despite commenting on the hot debate about whether 'umbrella clauses' should be interpreted broadly[43], decided that 'umbrella clauses' shall be

[36] *SGS v. Pakistan*, *supra note* 2, ¶167; A. Reinisch, Umbrella Clauses: Seminar on International Investment Protection, Winter Semester 5. 2006-2007, cited in G. Salatino, *Overview of Umbrella Clauses*, 13 Bus. L. Int'l 51, 56 (2012).

[37] Tai-Heng Cheng, *Power, Authority and International Investment Law*, 20 Am. U. Int'l L. Rev. 466, 473 (2005).

[38] *See*, *SGS v. Pakistan*, *supra note* 2; For an award repudiating the reference of all contractual claims to the breach of treaty but leaving a space for the cases in which the dispute arises not only from a breach of a contract but a breach of treaty rights and obligations, *see also*, *Joy Mining Machinery Limited v. The Arab Republic of Egypt*, ICSID Case No. ARB/03/11, Award on Jurisdiction, ¶81 (6 August 2004), *see at:* https://www.italaw.com/cases/590, (last visited: 6 November2017).

[39] *SGS v. Pakistan*, *supra note* 2, ¶167.

[40] Jonathan B. Potts, *Stabilizing the Role of Umbrella Clauses in Bilateral Investment Treaties: Intent, Reliance, and Internationalization*, 51 Va. J. Int'l L. 1006, 1016 (2011).

[41] Köşgeroğlu, *supra note* 13, 317.

[42] *El Paso Energy International Company v. The Argentine Republic*, , ICSID Case No. ARB/03/15, Decision on Jurisdiction, ¶70, 80, 82 (27 April 2006), *see at:* https://www.italaw.com/cases/382, (last visited: 6 November 2017).

[43] *Ibid*, ¶70.

interpreted narrowly. Without getting stuck on the arguments supporting the wording of 'umbrella clauses' in international investment treaties, the Tribunal expressed that it should be distinguished in each case whether an investment contract was breached by a sovereign or merchant state[44]. If a breach results from acts of sovereign states[45], such as indirect expropriations, foreign investors will be able to invoke IIAs. Such a distinction would prevent foreign investors' attempt to invoke international treaties for trivial issues such as delay in payments by state parties.[46]

To summarize the restrictive approach towards the implementation of 'umbrella clauses', arbitration tribunals are prone to assess the wording of 'umbrella clauses' on the case-to-case basis and use different techniques such as sovereignty issues, in order to restrict the scope of application of 'umbrella clauses'.[47]

2.2. Extensive Approach

Extensive implementations of 'umbrella clauses' take their inception from *SGS v. the Philippines case*, in which the Tribunal held that if the intention of parties was to exclude specific agreements between the host state and the investor and interpret the protection broadly, it could have been expressed in the following article.[48] The author considers it unnecessary to deepen the analysis of this case, but instead, in order to display the contradiction in case law of the ICSID, finds it useful to point out the view of the Tribunal six months before, in the *SGS v. Pakistan case*, in which the Tribunal looked for the intention of parties for a broad interpretation. In contrast, in this case, the absence of intention did not result in the restrictive implementation of the 'umbrella clause'.

Pursuant to the pioneer case brought against the Philippines, the case law of the ICSID was improving case by case so that in the case of *CMS v. The Argentine Republic*,[49] the Tribunal stated the possibility of commercial disputes

[44] *Ibid*, ¶80.

[45] In order to reach a conclusion about whether 'umbrella clauses' should be applied to a sovereign or merchant state's obligation, the Tribunal interpreted the 'umbrella clause' mentioned in Argentine-US BIT as *"[a]ll disputes resulting from a violation of a commitment given by the State as a sovereign State, either through an agreement, an authorisation, or the BIT."*(emphasis added) *Ibid*, ¶81; For the similar view, *see also*, Köşgeroğlu, *supra note* 13, 331.

[46] *El Paso Energy v. The Argentine supra note 41*, ¶81-2; *See also*, *Pan American Energy LLC, and BP Argentina Exploration Company v. The Argentine Republic*, ICSID Case No. ARB/04/8, Decision on Preliminary Objections, ¶109 (27 July 2006), *see at*: https://www.italaw.com/cases/808 (last visited: 6 November 2017).

[47] E. Whitsitt & N. Bankes, *The Evolution of International Investment Law and Its Application to the Energy Sector*, 51 Alta. L. Rev. 207, 235-6 (2013).

[48] *SGS v. The Philippines*, *supra note* 18, ¶118.

[49] *CMS Gas Transmission Company v. The Argentine Republic*, ICSID Case No. ARB/01/8, Award, ¶299 (12 May 2005), see at: https://www.italaw.com/cases/288, (last visited: 6 November 2017); For similar views, *see also*, *Bureau Veritas, Inspection, Valuation, Assessment and Control,*

to be elevated with the help of 'umbrella clauses' if there had been a significant interference by public authorities. Another tribunal in *Noble Ventures v. Romania case*,[50] built up its standpoint on a view that the practical content (*'effet utile'*) of the 'umbrella clause' should not get hurt by a limited interpretation,[51] thereby chose the plain implementation of the clause. Setting out the principle of *'effet utile'*, different Tribunals reached similar conclusions and found a firm nexus between investment contracts and treaties which reinforced contractual claims in turn.[52]

The legal doctrine and as a result of the reciprocal influence, the arbitration tribunals today support the extensive approach in the interpretation of 'umbrella clauses',[53] as well as state that if there is a breach of contract, the parties need not prove the breach of an international investment treaty additionally.[54] Though, such breaches are not, in the case law, accepted as equivalent to any breach of public international law or relevant IIA, but should be dealt with to the same effect.[55] The developing route of the understanding of 'umbrella clauses' was combined in the *SGS v. Paraguay case*[56], in which the Tribunal gave a preference to the *SGS v. the Philippines case*, in terms of the extensive implementation and interpreted the disputed clause,

BIVAC B.V. v. The Republic of Paraguay, ICSID Case No. ARB/07/9, Decision of the Tribunal on Objections to Jurisdiction, ¶141 (29 May 2009), *see at:* https://www.italaw.com/cases/179, (last visited: 7 November, 2017); For a recent similar approach, *see also*, *Bosh International, Inc and B&P Ltd Foreign Investments Enterprise v. Ukraine*, ICSID Case No. ARB/08/11, Award, ¶252 (25 October 2012) *see at:* https://www.italaw.com/cases/documents/1564, (last visited: 8 November 2017).

[50] *Noble Ventures, Inc v. Romania*, ICSID Case No. ARB/01/11, Award, ¶51-6 (12 October 2005), *see at:* https://www.italaw.com/cases/documents/748, (last visited: 7 November, 2017).

[51] Köşgeroğlu, *supra note* 13, 319-20; For the similar approach, *see also*, Patrick Dumberry, et al, International Investment Law: The Sources of Rights and Obligations,' in International Investment Contracts, ed. Tarcisio Gazzini, et al. 238. (2012).

[52] *See*, *Sempra Energy International v. The Republic of Argentine*, , ICSID Case No. ARB/02/16, Decision on Objections to Jurisdictions, ¶101 (11 May 2005), see at: https://www.italaw.com/cases/1002, (last visited: 7 November 2017); For an original nature of an extensive implementation of 'umbrella clauses', *see also*, *Eureko v. Poland*, *supra note* 33, ¶248-9; To look through the list of other related case law of the ICSID, *see also*, Köşgeroğlu, *supra note* 13, 321, n. 1211.

[53] Katherine Jonckheere, 'Practical *Implications from an Expansive Interpretation of Umbrella Clauses in International Investment Law*, 11 S.C. J. Int'l L. & Bus. 143, 151 (2015).

[54] Schreuer, *supra note* 4, 255.

[55] *SGS v. The Philippines*, *supra note* 18, ¶126, 128. The Tribunal in this case, however, also gave a reference to 1988 the United Nations Conference on Trade and Development (UNCTAD) Study in order to substantiate its argument, *see*, J. Honlet & G. Borg, *The Decision of the ICSID Ad Hoc Committee in CMS v. Argentina Regarding the Conditions of Application of an Umbrella Clause: SGS v. Philippines Revisited*, 7 The Law and Practice of International Courts and Tribunals: A Practitioners' Journal 1, 13 (2008).

[56] *SGS Société Générale de Surveillance S.A. v. The Republic of Paraguay*, ICSID Case No. ARB/07/29, Decision on Jurisdiction, ¶176 (12 February 2010), see at: https://www.italaw.com/cases/1016, (last visited: 7 November, 2017).

once again as an additional protection the contracting parties agreed upon for the foreign investor. From our point of view, too much extensive implementation of 'umbrella clauses' can also harm the heartbeat of this clause, its *'effet utile.'* The more obligation and commitments contracting states undertake, the more risks accompany their undertakings, especially, the unilateral ones.

3. Unilateral Commitments: How Big Is the Shelter that the Article 10(1) of the Energy Charter Treaty Ensures?

The question whether 'umbrella clauses' protect or exclude each commitment of states is hitherto open to a hot debate. Investors' legitimate expectations become an issue, in this regard. As we have discussed in the previous paragraphs of this research, the wording of 'umbrella clauses' sometimes can be too broad, by saying for example, "contracting parties shall observe all obligations with regard to investments", and sometimes, relatively broad, "contracting parties shall observe all obligations it may have entered into with regard to investments." These two wordings differ from each other, as the shelter the 'umbrella clause' provides in the latter example is not very large. The latter example stems from the *CMS v. Argentina case*, in which the Tribunal concentrated on the consensual obligations by taking into account the wording *"entered into."*[57] If the former formulation is accepted, it will influence the *ratione personae* of 'umbrella clauses' as well, which is out of the topic of our research. However, the author cannot help but state that such a broad interpretation would even enable foreign investors who are actually an indirect party of investment contracts, and in addition, shareholders of an injured company, in which they own an interest,[58] to invoke 'umbrella clauses' of IIAs against contracting parties.[59]

Opinions of different Tribunals and the case law, in general, seem to be in a mess. While some cases were concluded without any tolerance for the unilateral promises, some of them were willing to include. To illustrate, the tribunals in the *SGS v. The Philippines* and *El Paso v. Argentina* excluded unilateral commitments and regulatory measures because of their general character.[60] On the other hand, in the cases of *Sempra v. The Argentine Republic*,

[57] Honlet& Borg, *supra note* 54, 18; For an opposite view extending the wording "entered into" to investment authorizations and permissions, *see also*, E. Gaillard and M. McNeill, The Energy Charter Treaty, in Arbitration under International Investment Agreements: A Guide to the Key Issues, ed. K. Yannaca-Small 48. (2010).

[58] In the legal doctrine, one solution for discarding indirect parties of investment contracts made with host states is sought in the formulation of 'umbrella clauses' by inserting "obligations assumed with respect to investors." Shotaro Hamamoto, *Parties to the 'Obligations' in Obligations Observance ('Umbrella') Clause*, 30 ICSID Review 449, 464 (2015).

[59] For the study of *ratione personae* in this regard, and unilateral commitments, *see*, Köşgeroğlu, *supra note* 13, 334-7.

[60] Jonckheere, *supra note* 52, 159.

LG&E Energy Corp. v. The Argentine Republic and *Enron Corp. v. The Argentine Republic,* the decisions of the Tribunals were more or less similar as they all recognized unilateral undertakings under the 'umbrella clause' protection.[61] Finally, the decision of the Tribunal in the case of *SGS v. Paraguay*[62] can be categorized as an improvisation among these decision, concerned by the fact that the Tribunal was hesitant when it referred oral and written commitments of the state to the 'umbrella clause' at the preliminary review but did not in its final decision.

Bearing in mind that the case law is inclined to include unilateral commitments in the shelter of 'umbrella clause' protection, it is not straightforward to draw an exclusive conclusion, rather than inclusive. However, in the author's opinion, they should be excluded. The consensus of parties to investment contract should be a clue to mark the boundaries of the term "*any obligations*." When the tribunals are almost unanimously exclude purely commercial disputes from the shelter of the protective umbrella, the author, relying on *'argumentum a fortiori',* does not perceive it reasonable to include unilateral regulatory commitments in which a consensus is not a constructive element. In this plethora of cases in favour of more extensive interpretations, the author is seeking an explanation for such kind of implementation of the tribunals' in the wording of 'umbrella clauses' in IIAs.

C. Opt-Out: Article 26(3)(C) of Energy Charter Treaty

The 'umbrella clause' comprised in Article 10(1) of the ECT is not absolute, and its effect can be restricted by contracting states. Article 26(3)(c) of the ECT entitles its contracting parties to derogate from the effect of the last sentence of Article 10(1). While the first sentence of Article 26(3)(b) provides a general derogation rule and enables the members listed in Annex ID to decline their consent to the dispute settlement system with a condition that the investor previously files the application to another dispute settlement procedure, Article 26(3)(c) which is read as follows, is directly related to Article 10(1):

> "[A] Contracting Party listed in Annex IA do not give their unconditional consent to international arbitration in regard to

[61] *Sempra v. The Republic of Argentine*, *supra note* 51, ¶314; *LG&E Energy Corp., LG&E Capital Corp., and LG&E International, Inc .v. Argentine Republic,* , ICSID Case No. ARB 02/1, Decision on Liability, ¶174-5 (3 October 2006), see at: https://www.italaw.com/cases/documents/623, (last visited: 12 November 2017); *Enron Corporation and Ponderosa Assets, L.P. v. Argentine Republic,* ICSID Case No. ARB/01/3, Award, ¶277 (22 May 2007), *see at:* https://www.italaw.com/cases/401, (last visited: 12 November 2017).

[62] The Tribunal did not examine this question on merits because even if there was such a breach, *"[t]he breach would not result in any additional liability on behalf of the Respondent,"* (emphasis added) *see*, *SGS Société Générale de Surveillance S.A. v. The Republic of Paraguay*, ICSID Case No. ARB/07/29, Award, ¶158 (February 10 2012), see at: (last visited: November 8, 2017).

> disputes arising out of the alleged breaches of the obligation of the last sentence of Article 10(1)."

In principle, foreign investors do not need to bring their case before domestic courts in order to benefit from international arbitration.[63] In energy-related *Petrobart v. The Kyrgyz Republic case*[64], while applying Article 26 of the ECT to the case, the Tribunal expressed the same view that the submission of the dispute to local courts cannot prevent the investor's right to bring the case before international arbitration. However, as indicated in Article 26(3)(c), the contracting parties can obviously shut the doors of international arbitration to foreign investors as far as they wish, by simply derogating from the effect of 'umbrella clause' in the ECT. The countries which derogated from this clause are Australia, Canada (although did not sign the ECT), Hungary and Norway.[65]

As it is clear from the wording of the Article 26(3)(c), although 'umbrella clauses' provides a wide protection for investors in terms of the breaches of contractual obligations, this additional protection can be opted out by contracting parties. The author comprehends these provisions to the effect that contracting parties should have known about their right to derogate from the effect of the 'umbrella clause' comprised in the ECT, thus if they did not, it would be considered an implicit consent for the contractual breaches to be disputed against them within the international arbitration mechanisms of the ECT.

Conclusion

Due to the discrepancies between the decisions of tribunals with regard to the interpretation of 'umbrella clauses', it is strenuous to reach a uniform conclusion. Too much extensive interpretation would cause an excessive workload of arbitration tribunals. It would be contrary to the intention of contracting parties while drafting IIAs and to the nature of 'umbrella clauses'. Because this clause is an exception to the rule of customary international law that delineates the difference between public international law and private law, despite it is not absolute.

The author supports the view that 'umbrella clauses' should at least be applied to some obligations, in order to preserve its *'effet utile.'* The last sentence of Article 10(1) of the ECT applies only to contractual obligations of

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[63] Kamal Gadiyev, *Arbitration of Energy-Related Disputes under the Energy Charter Treaty*, 8 Global Jurist 1, 8 (2008).

[64] Petrobart Limited v. The Kyrgyz Republic, SCC Case No. 126/2003, Arbitral Award, 55 (29 March 2005), *see at:* https://www.italaw.com/cases/documents/826, (last visited: 11 November 2017).

[65] K. Yannaca-Small, *Interpretation of the Umbrella Clause in Investment Agreements*, OECD Working Papers on International Investment, 5 (2006), *see at:* http://dx.doi.org/10.1787/415453814578, (last visited: 6 November 2017).

contracting states that we exclude unilateral commitments. To the meaning of the ECT, these contractual obligations must be made with investors and in relation with the investments which in turn need to consider the definitions of the ECT regarding the "investor" and "investments". The right to file the dispute to the arbitration tribunal under ECT does not affect the investor's right to domestic remedies. However, if an investor's host state has derogated from the last sentence of Article 10(1) under Article 26(3)(c), the investor will only be able to invoke contractual remedies – either domestic courts or arbitration agreed in the investment contract.

In any case, the wording in investment treaties in regard to 'umbrella clauses' deserves a specific attention. Main objectives of IIAs can be attached an importance regarding that if they aim to protect foreign investors or demonstrate a balanced protection. Although we do not support the excessively extensive interpretation of 'umbrella clauses,' with a single signature, states are still free to bind themselves with each commitment they assume with regard to investments. Hence, pursuant to the inclusion of the 'umbrella clause,' investors may be able to benefit from its 'elevator effect', however, it is always important to press the correct button that will elevate your investment contract to the treaty level.