

# **Umbrella Clauses in Bilateral Investment Treaties (BITs) and Impact on Developing Countries**

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**Abstract:** Bilateral Investment Treaties primarily regulate the investment relationships between the investors and the host states. There are more than 2500 BITs but there is no clear guideline regarding the scope and characteristics of the umbrella clause and the arbitral tribunals issue where gives and conflicting decisions. When there is a BIT between two developed countries, the umbrella clause does not create many problems but when it is with any developing countries, it creates a discriminatory agreement and establishes an inequitable relationship because of the social, economic, cultural, and unstable political status of the developing countries. This paper discusses two issues regarding the umbrella clause namely, (I) Whether does the umbrella clause establish a fair relationship between the investor and the receiving developing country.? (II) How can the umbrella clause can positively play a role in considering the reality of the conditions of the developing states This is a very new area considering the perspective of the developing countries never discussed before. This paper will help the future policymakers of the developing countries to make BITs that will not only consider the situations of the developing countries but also ensure trust in the investors for the protection of their property.

**Keywords:** Evolution, Umbrella clause, BITs, Developing Countries, International Investment Treaties

## **1. Introduction**

The Umbrella clause in Bilateral Investment Treaties (BITs) is a controversial clause from the very beginning of the inclusion of the clause in BITs. Though there was controversy regarding the clause has been included in different BITs from the decade 1960s as it was invented in the 1950s. There was a direct influence of the western philosopher and the draft “Convention on Investment Abroad” formulated by Hermann Josef Abs and Sir Hartely Shawcross which is also known as the “Abs-Shawcross Draft”.<sup>1</sup> Article 2 of the OECD Draft is an umbrella clause that provides

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<sup>1</sup> Jarrod Wong, ‘Umbrella Clauses in Bilateral Investment Treaties: Of Breaches of Contract, Treaty Violations, and the Divide Between Developing and Developed Countries’ (2006) 14 *George Mason Law Review* 135.

as follows: "Each Party shall at all times ensure the observance of undertakings given by it in relation to property of nationals of any other Party."<sup>2</sup> There was no representation of perspectives of the developing states who are in most cases the host states at the beginning. However, the impacts and functions of the umbrella clauses did not attract attention vastly from the philosophers of the world until the starting of the 21<sup>st</sup> Century as the conflict between the investors and host states used to be solved by different means such as mutual understanding, using local courts even attempting to invoke jurisdiction of the International Court of Justice. The issue has become more controversial when two arbitral tribunals have given two different interpretations of the 'Umbrella Clause' and later, different tribunals have given interpretations according to their own which makes the clause reason of very much uncertainty in the relationship between investors and investment. However, to interpret the umbrella clause the tribunal or the author only focused on the investors and didn't give a look into the fact of the developing countries. In recent times, many countries leaving the umbrella clause from the BITs. The very truth is that the investors who make BITs with the developing states get the privilege of setting different provisions in the treaty and the developing states to ensure and attract investment agree with the provisions. Afterward, if a developing country becomes a host state and ensures the broad obligations, it becomes overburdening for them which violates the international customary law and it is inequitable. This paper did not focus on the impact on the developed countries when they are host countries and have included umbrella clauses in their BITs. It has focused on the perspective of the developing countries when they are host states in an investment treaty.

Different literature deals with different perspectives of the umbrella clause in BITs but there is no indication of the perspective of the developing countries purely or any guidelines for umbrella clauses to make balanced BITs between the investors and the developing states. Some authors supported the restrictive view in interpreting the umbrella clause for different reasons based on the language and influenced by the previous decisions. In this paper, it will be searched whether the umbrella clauses ensure equitable relationships between the investors and host developing countries. Then the author tried to find how the umbrella clause can ensure the protection of the investors as well as does not become an overburden for the developing countries.

## **2. Objectives of the Study:**

The umbrella clause informally took place in the international investment law in the 1950s and later it is supported by other different authors and international conventions and has become part and parcel of the international investment treaties.

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<sup>2</sup> Organisation for Economic Co-operation and Development, *Draft Convention on the Protection of Foreign Property and Resolution of the Council of the OECD on the Draft Convention* (OECD Publication No 23081, 12 October 1967) reprinted in (1968) 7 *International Legal Materials* 117.

Though from the very beginning, there is a continuing debate that this clause gives more favor to the investors who are in reality the developed states of the world. At the beginning of the twenty-first century, two conflicting decisions from the arbitral tribunals namely, *SGS v. Pakistan*<sup>3</sup> and *SGS v. Philippines*<sup>4</sup>, have made this debate very much clear, and the later different tribunal has decided their case according to their principle as in international law the decisions are not binding on the later tribunals. So, different authors also discussed the controversy from their perspectives and have given different solutions for making a balance. Some argued that the umbrella clause is indeed vastly needed for the protection of the investors. Few authors talk about the perspective of the developing states. So, in this paper, an effort has been made to reflect the perspectives of the developing countries and to find the answer to whether the umbrella clause is ensuring an equitable relationship between the developed and the developing countries. The purpose is to find some solutions by which the developing countries can also run their investment relationship with the investors as well as protect the government of the developing countries.

### 3. Methodology of Study

This study adopts a qualitative doctrinal research method, relying on the analysis of treaties, arbitral awards, and scholarly writings relevant to umbrella clauses in bilateral investment treaties. A comparative approach is used to examine variations in treaty language and to contrast the divergent interpretations adopted by arbitral tribunals, particularly in cases such as *SGS v. Pakistan* and *SGS v. Philippines*.

All information, including treaty texts, case law, and academic commentary, has been sourced from publicly available documents, official databases, and published literature, with citations provided in footnotes and the bibliography. The study synthesizes these materials to evaluate whether umbrella clauses create equitable obligations for developing countries and to identify potential reforms.

This methodological approach allows for a systematic examination of legal doctrine and arbitral practice while incorporating the broader policy context affecting developing states.

### 4. Meaning of the Umbrella Clause

An umbrella clause is a clause in any bilateral investment treaty (BIT) by which the parties agree to obey all the obligations owed to the foreign investors. It gives the investor more advantage than the host state because the umbrella clause permits the investor to argue that the issues which are ordinarily dealt with by the local law and jurisdiction to be declared as a breach of an investment treaty as a result of the

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<sup>3</sup> *Societe Generale de Surveillance SA v Islamic Republic of Pakistan*, ICSID Case No ARB/01/13, Award (8 September 2003) 361–63.

<sup>4</sup> *SGS Société Générale de Surveillance SA v Republic of the Philippines*, ICSID Case No ARB/02/6, Decision on Jurisdiction (29 January 2004) para 127.

umbrella clause.<sup>5</sup> This clause makes the investor capable to elevate all the disputes with the host state to the international forum under the umbrella clause of the BIT.

According to the definition of Professors Dolzer and Schreuer, “An umbrella clause is a provision in an investment protection treaty that guarantees the observation of obligations assumed by the host State vis-à-vis the investor.”<sup>6</sup>

The Umbrella clause is not uniform always in its construction in all BITs. The wording of the BITs is one of the reasons for justifying different interpretations. A common formulation appears in several treaties, for example BIT is defined by the British Model as “Each contracting party shall observe any obligation it may have entered into about investments of nations or companies of the other contracting party.”<sup>7</sup> Article 10(1) of the Energy Charter Treaty 1994 has also a similar content as it has in its umbrella clause in the British Model Treaty. Example of umbrella clauses: Article II (2) of the BIT between Romania and the US provides that each party shall observe obligations relating to investments made by investors of the other party.

Likewise, the UK–Argentina BIT and several other treaties adopt similarly broad language, reinforcing the expectation that contractual or statutory commitments made by the host state may fall under treaty protection.<sup>8</sup> Article 2(2) of the UK–Argentina BIT provides that “Investments of investors of each Contracting Party shall at all times be accorded fair and equitable treatment and shall enjoy protection and constant security in the territory of the other Contracting Party.”<sup>9</sup> This broad formulation is echoed in other BITs as well. For example, Article 3 (1) of the Bangladesh - Germany BIT (1981) provides that: “Investments by nationals or companies of either Contracting Party shall enjoy full protection as well as security in the territory of the other Contracting Party.”<sup>10</sup> Both provisions illustrate how BITs commonly use general language to impose wide-ranging obligations on host states, thereby expanding the protective scope available to foreign investors.

Again, Article 3(1) of the Bangladesh- Austria BIT (2000) provides that: “Each Contracting Party shall accord to investments by investors of the other Contracting

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<sup>5</sup> Sanderson B, ‘Umbrella Clauses in Investment Treaty Arbitration’ (LexisNexis, 2025) <<https://www.lexisnexis.co.uk/legal/guidance/umbrella-clauses-in-investment-treaty-arbitration>> accessed 31 March 2025.

<sup>6</sup> Jean-Christophe Honlet and Guillaume 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’ (2008) 7,1, 32, quoting R Dolzer and C Schreuer, *Principles of International Investment Law* (OUP 2008) 153.

<sup>7</sup> British Model Bilateral Investment Treaty, art 2(2).

<sup>8</sup> *ibid*

<sup>9</sup> *ibid*

<sup>10</sup> Bangladesh–Germany Bilateral Investment Treaty (1981) <<https://investmentpolicy.unctad.org/international-investment-agreements/treaty-files/264/download>> accessed 31 March 2025.

Party fair and equitable treatment and full and constant protection and security.”<sup>11</sup> Recently, in Bangladesh - Turkey BIT (2012)<sup>12</sup> there is no provision like an umbrella clause but Bangladesh - Denmark BIT (2009)<sup>13</sup>, and Bangladesh- India BIT (2009) bears an umbrella clause.

Though the wording of the provision may be different in different BITs, the aim is similar. The clause aims to protect the foreign investor. If there is an umbrella clause in a contract, it means that some contractual obligations which are to be governed by domestic law will create an international obligation for the host state and the investor will get the protection of international investment law.<sup>14</sup> So, a breach of contractual obligations becomes a breach of a BIT and it attracts the protection of international foreign investment law. This creates confusion between private law disputes and public law disputes.<sup>15</sup>

## 5. Discussions

The umbrella clause is criticized from the very beginning of its inclusion. The controversial decisions of the arbitral tribunals have made the clause a great concern for the academicians in the field of research as well as for the policymakers of the developing countries as it creates a great dilemma for them to decide what to do for attracting foreign investment. In many cases, the developing countries vastly depend on the development based on foreign investment. Different practices which are building a discriminatory and inequitable relationship between the investors and the developing countries is discussed below.

### (a) Ignorance of the perspective of the Developing Countries regarding the umbrella clause

The ways by which the perspective of the developing countries has been ignored is described here:

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<sup>11</sup>Bangladesh–Austria BIT (2000) <<https://investmentpolicy.unctad.org/international-investment-agreements/treaties/bilateral-investment-treaties/226/austria---bangladesh-bit-2000>> accessed 31 March 2025.

<sup>12</sup>Bangladesh–Turkey BIT (2012) <<https://investmentpolicy.unctad.org/international-investment-agreements/treaties/bilateral-investment-treaties/388/bangladesh---turkey-bit-2012>> accessed 31 March 2025.

<sup>13</sup>Bangladesh–Denmark BIT (2009) <<https://investmentpolicy.unctad.org/international-investment-agreements/treaties/bilateral-investment-treaties/368/bangladesh---denmark-bit-2009>> accessed 31 March 2025.

<sup>14</sup> AC Sinclair, ‘The Origin of the Umbrella Clause in the International Law of Investment Protection’ (2005) 20(4) *Arbitration International* 411, cited in Surya P Subedi, *International Investment Law: Reconciling Policy and Principle* (Hart 2008) 104.

<sup>15</sup> MD Nolan and EG Baldwin, ‘The Treatment of Contract-Related Claims in Treaty-Based Arbitration’ (2006) 21(6) *Mealey’s International Arbitration Report 1-8*, cited in Surya P Subedi, *International Investment Law: Reconciling Policy and Principle* (Hart 2008) 105.

## Controversial Decisions on Umbrella Clause by Arbitral Tribunals

Before World War II, the domestic court was the main forum for investment disputes and the investors had little trust in it. The developed countries tried to establish international norms, institutions, and international enforcement procedures to apply the umbrella clause at the level of international law. The ICSID, 1966, and the MIGA, 1985 focused on the internationalization of the terms used in international investment protection law. Then, International arbitral tribunals increased the protection chain through interpretations, firstly, the arbitration was only contract-based later it became treaty-based but only inter-governmental. Finally, it became a treaty-based direct investor and state arbitration.<sup>16</sup>

Though the developed states included a provision with a similar pattern to bind the host state for violation of any provision of the contract and it is named an umbrella clause by various ICSID tribunals, The clause didn't get huge attention before 2003. The question of jurisdiction of the international arbitral tribunal over contractual counterclaims and the question of ousting or preceding contractual jurisdiction clauses by the jurisdiction of treaty-based tribunals were never examined before the two SGS cases in 2003. In this year, two conflicting decisions regarding the umbrella clause in this century by ICSID are the reason for getting huge attention from the different levels of scholars.

The first case was the **SGS vs. Pakistan**<sup>17</sup> where the Swiss company SGS signed a contract with the Republic of Pakistan in 1994 to provide "pre-shipment inspection" ("PSI").<sup>18</sup> Services related to specific products for Pakistan. ("PSI Agreement"), SGS has promised to control goods entering Pakistan with the aim of increasing customs revenue by ensuring that goods are properly classified for customs purposes.<sup>19</sup> However, a few years after the agreement was signed, Pakistan was dissatisfied with SGS.<sup>20</sup> Performance and contract were terminated by Pakistan. Afterward, Pakistan has begun arbitration proceedings in Pakistan under article 11 of the PSI contract. It defines that the dispute arising from the PSI Agreement will be settled by the following arbitration which is Pakistan's Arbitration Law.

However, SGS itself has started the process in another forum. It filed an arbitration claim with ICSID, claiming that Pakistan's actions under the PSI Agreement violated its obligations under the PSI Agreement.<sup>21</sup> Switzerland Pakistan BIT signed by both countries, in particular, SGS argued that Pakistan's actions constitute a breach of various BIT clauses that set substantive standards for the handling of investments, including Pakistan, for example, "Protect" the requirements under Article 4 (1) or Article 4 (2) Ensuring a "fair and equitable" treatment of Swiss investment in

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<sup>16</sup> n(20) 200.

<sup>17</sup> n (3).

<sup>18</sup> Ibid., para 11.

<sup>19</sup> Ibid., para 11.

<sup>20</sup> Ibid., para 16.

<sup>21</sup> Ibid., para 153.

Pakistan.<sup>22</sup> In addition, SGS argued that under BIT Pakistan is responsible for all breaches of the PSI Agreement due to the BIT Comprehensive Clause (Article 11), which provided: "Either Contracting Party shall constantly guarantee the observance of the commitments it has entered into with respect to the investments of the investors of the other Contracting Party."<sup>23</sup> SGS argued that the contract claim was automatically "upgraded" to a BIT claim as the clause required Pakistan to "permanently guarantee" the investment "Obligations" for Swiss investors. This includes all contractual obligations.<sup>24</sup> Therefore, SGS claimed that the ICSID court had jurisdiction. About contractual disputes.<sup>25</sup> The ICSID tribunal observed that breach of private contract does not by nature elevate to the level of violations of the international treaty.<sup>26</sup>

On the contrary, the second case was *SGS v Philippines*<sup>27</sup> where a different panel than before found that contractual responsibilities are covered by a comparable umbrella provision to that included in the Swiss-Philippines BIT. "Each contractual party shall observe whatever obligation it has assumed concerning specific investments in its territory by investors of the other contracting party," according to Article X (2) of this BIT's umbrella clause. The tribunal determined that all commitments and undertakings originating from contracts entered into by the host state are covered by article X (2) of the BIT because of this umbrella provision.<sup>28</sup> The decision of the second tribunal increased the use of the ICSID arbitral tribunal for any dispute between an investor and the host countries. Over the years the use of international arbitration has increased rather than domestic litigation in the field of international investment law in this century.

Later different tribunals in different cases have taken view according to their own considerations as in international tribunal the tribunals are not bound to follow the principle decided before. Some has supported the view taken by the tribunal in *SGS vs Pakistan* case and some other has hold similar view as observed in *SGS vs Philippines* case. Though some tribunals discussed from other grounds also to deal with the umbrella clause. In *Joy Mining Machinery Limited v. The Arab Republic of Egypt*, the Tribunal explained the "umbrella clause" in the same way that the *SGS v. Pakistan* tribunal did, stating that the disputes at issue, which related to the release of bank guarantees, were commercial and contractual disputes to be resolved through the contract's mechanism. It stated that:

“[i]n this context, it could not be held that an umbrella clause inserted in the treaty, and not very prominently, could have the effect of transforming all contract disputes into investment disputes under the Treaty unless of course there would be a clear

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<sup>22</sup> Ibid., para 35.

<sup>23</sup> Ibid., para 97-99.

<sup>24</sup> Ibid., 53-54, 98-99.

<sup>25</sup> Ibid., para 53-54.

<sup>26</sup> n (3).

<sup>27</sup> n (4).

<sup>28</sup> n (4).

violation of Treaty rights and obligations or a violation of contract rights of such a magnitude as to trigger the Treaty protection, which is not the case. The connection between the Contract and the Treaty is the missing link that prevents any such effect. This might be perfectly different in other cases where that link is found to exist, but certainly, it is not the case here.”<sup>29</sup>

In *El Paso Energy International Company v. The Argentine Republic*,<sup>30</sup> the tribunal held a different view from the *SGS v. Philippines* that if there is any ambiguity in the terms of the treaty, the issues will be resolved in favor of the foreign investors. It also didn't agree with the *SGS v. Pakistan*. On contrary, it took a balanced approach to interpreting the investment treaty, recommending that "both State sovereignty and the State's responsibility to create an adapted and evolutionary framework for the development of economic activities, as well as the necessity to protect foreign investment and its continued flow" be taken into account.<sup>31</sup> It rejected the wider meaning and adopted a narrow meaning that

“Given the necessity to distinguish the States a merchant, especially when it acts through instrumentalities, from the States as a sovereign, the Tribunal considers that the “umbrella clause” in the Argentine-US BIT...can be interpreted in the light of Article VII(1) which includes among the investment disputes under the Treaty all disputes resulting from a violation of a commitment given by the State as a sovereign State, either through an agreement, an authorization, or the BIT interpreted this way, the umbrella clause read in conjunction with Article VII, will not extend the Treaty protection to breaches of an ordinary commercial contract entered into by the State or a State-owned entity, but will cover additional investment protections contractually agreed by the State as a sovereign – such as stabilization clause – inserted in an investment agreement.”<sup>32</sup>

The tribunal observed that the broad interpretation of the umbrella clauses would have “a far-reaching consequence, quite destructive of the distinction between national legal orders and the international legal order”.

The case *Pan American Energy LLC and BP Argentina Exploration Company v. Argentina Republic* took the same route as the *El Paso* arbitration. The use of the umbrella clause was limited to contracts negotiated by an investor and the State acting as a sovereign, according to the Tribunal in *CMS Gas Transmission Company v. the Republic of Argentina*.<sup>33</sup>

However, there are also some other decisions that are contrary to the decisions alike *SGS vs Pakistan*.<sup>34</sup> In *SGS vs the Philippines*, the tribunal focused on the language

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<sup>29</sup> n (4) Para 81.

<sup>30</sup> *El Paso Energy International Company v Argentine Republic*, ICSID Case No ARB/03/15, Decision on Jurisdiction (27 April 2006).

<sup>31</sup> *Ibid.* para. 70.

<sup>32</sup> *Ibid.*, para 81.

<sup>33</sup> *CMS Gas Transmission Company v Argentine Republic* ICSID Case No ARB/01/8 (Award, 12 May 2005).

<sup>34</sup> *SGS Société Générale de Surveillance SA v Islamic Republic of Pakistan* ICSID Case No ARB/01/13.

and observed that the language of the two treaties is not the same. the tribunal took a wider view regarding the scope of the umbrella clause that if there is any exclusive jurisdiction vested by contract on any other tribunal such as a domestic court or a contractual arbitral tribunal, then also ICSID tribunal will have primary jurisdiction.

The *Partial Award in Eureka B. V. v. Poland*<sup>35</sup> examined the question of the "umbrella clause" included in the Netherlands-Poland BIT in great detail and it focuses on the ordinary meaning of the clause as mentioned in Article 31, paragraph 1 of the Vienna Convention. It concluded that the contractual obligations were subject to the jurisdiction of the Tribunal. It stated that:

"Any responsibilities it may have entered into with respect to particular overseas assets are not hidden." The verb 'shall observe' is both obligatory and categorical. 'Any' obligations is a broad term that encompasses not only obligations of a certain type, but all obligations entered into with respect to investments made by investors from the other Contracting Party."<sup>36</sup>

In *Noble Ventures, Inc v. Romania*, the tribunal considered whether the contractual duties amounted to international obligations because of the "umbrella clause" in the US-Romania BIT, concluding that Article II(2)(c) of the BIT intended to generate such requirements. It's also worth noting that when parties negotiate a bilateral investment treaty, they may include an exemption to the separation of state and municipal obligations under international law.

It is reasonable to say that the function and scope of the umbrella clause are decided case to case differently based on the intention and wording of the clause. However, in nowhere there is any mention of the perspective of the developing countries. The different explanations of the tribunals have created confusion regarding the umbrella clause and the original intention of the framer of the umbrella clause is in no way which is present at this moment. It expanded from the original intention and the present stage is inequitable as well as discriminatory against the developing countries which are not acceptable in customary international law. The tribunal must need to be constant regarding the characteristics of the umbrella clause otherwise the investment disputes will always be in favor of the investors and the developing countries will be deprived of justice and injustice through law is not bear a good future in any field.

Though there is no exact meaning of umbrella clauses, it is proved that the umbrella clause always added something rather than subtracting something from the range of protection received by the investors in the host developing countries under customary international law and the investment laws before. The inclusion of the umbrella clause in BITs was to create and maintain favorable conditions for the investor.

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<sup>35</sup> *Eureka B.V. v Poland*, Partial Award (19 August 2005) <<http://www.investmentclaims.com/decisions/Eureka-Poland-LiabilityAward.pdf>> accessed 31 March 2025.

<sup>36</sup> *Ibid.* para. 246.

Different decisions and authors have given different opinions regarding the scope of the umbrella clause. However, still, there is no clear guideline regarding the scope or function of the umbrella clause. Different arbitral tribunals hold their views depending on the language of the specific BITs. Some supported the restrictive view and some supported the wide view and some other tribunals tried to make a balance.

### **Expanding the Scope of Umbrella Clause:**

Developing countries frequently face structural economic and institutional constraints and therefore rely heavily on foreign investment to support development objectives.<sup>37</sup> To attract capital, host states often agree to broad treaty protections and contractual concessions requested by investors, which can include umbrella-clause language that elevates certain domestic commitments to international obligations.<sup>38</sup> Arbitral practice demonstrates the practical consequences of such language. Some tribunals have taken an expansive view, allowing investors to convert contractual breaches into treaty claims under umbrella clauses (e.g., *SGS v. Philippines*, ICSID Arb. No. ARB/02/6 (2004); *Eureko v. Poland*, Partial Award (2005); *Noble Ventures v. Romania*), while others have adopted a restrictive approach that limits umbrella clauses to obligations assumed by the State in its sovereign capacity (e.g., *SGS v. Pakistan*, ICSID Arb. No. ARB/01/13 (2003); *Joy Mining v. Egypt*; *El Paso v. Argentina*, Decision on Jurisdiction (2006)). This divergence has produced uncertainty about whether umbrella clauses can be used to invoke obligations owed to other investors or to bypass contractual forum-selection clauses (see *SGS v. Philippines*; *Eureko v. Poland*), raising concerns that tribunals sometimes decide primarily on treaty wording without sufficiently accounting for the economic and institutional realities of developing host states.<sup>39</sup> Given this jurisprudential split, scholarly commentators and policymakers have warned that broad umbrella-clause interpretations may grant disproportionate leverage to investors and undermine domestic dispute-resolution mechanisms, thereby creating potential imbalances in investor–state relations that are especially acute for developing countries.<sup>40</sup>

The language and position of the umbrella clause in the treaty provide the possibility of interpretation of the scope and effect of the umbrella clause and this clause is becoming a big problem for the developing countries for arbitrary use by the developed countries as there is less possibility of showing stronger opinion by the developing countries.

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<sup>37</sup> Rudolf Dolzer and Christoph Schreuer, *Principles of International Investment Law* (OUP 2008).

<sup>38</sup> Anthony Sinclair, 'The Origins of the Umbrella Clause in the International Law of Investment Protection' (2004) 20 *Arbitration International* 411.

<sup>39</sup> Michael D Nolan and Edward G Baldwin, 'The Treatment of Contract-Related Claims in Treaty-Based Arbitration' (2006) 3(5) *Transnational Dispute Management* 1.

<sup>40</sup> Jarrod Wong, 'Umbrella Clauses in Bilateral Investment Treaties: Of Sanctions, Remedies and National Court Jurisdiction' (2006) 14 *George Mason Law Review* 677.

Some umbrella clauses refer exclusively to the country's obligations as well as obligations between private individuals. Article 10 of the Australia-Poland Bilateral Investment Treaty of 1991, for example, states that: "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 about an investment is respected".<sup>41</sup>

Using "shall observe" is a common factor in the umbrella clauses. For example, Article 8(2) of the German Model BIT 1991(2) reads: "Each Contracting Party shall observe any obligation it has assumed concerning investments in its territory by nationals or companies of the other Contracting Party".

The position of the umbrella clause in the BIT also creates varied impacts on the treaty practice. In some of the BITs where the clause is used as substantive protections, others used it as only dispute resolution clauses. However, several others used it in a separate place than the substantive protections and before the dispute resolution clauses such as the German Model BITs which place the umbrella clause in Article 8.<sup>42</sup>

It seems that there is no uniform place for the umbrella clause and this creates also confusion among the countries regarding the scope of the umbrella clause when they are coming into force. The Tribunal in *SGS v Pakistan* believed that the Swiss-Pakistan BIT's umbrella provision was towards the conclusion of the document and that it was not a substantive requirement. However, the *SGS v Philippines* Tribunal opined that the position of the clause may have some weight and that's why the interpretation of the fact is not decisive.

Though the traditional foreign investment law is based on the principle of non-discrimination, the umbrella clause gives rise to discrimination against domestic investors. As foreign investment is more secure, the local investors also prefer to invest in other countries. According to a concept paper submitted by the EU to the WTO's working group on trade and investment<sup>43</sup>, many countries trying to attract foreign investors by creating reverse discrimination against their local companies. To save the local companies the developing states themselves need to come forward and have a non-discriminatory international investment law.

### **Inadequate Approach in interpreting the Umbrella Clause Ignoring Difficulties Faced by Developing Countries:**

The umbrella clause is interpreted depending on the intention of the investors and that's created a significant number of complexities in the arena of investment law. There is a pressing need to re-conceptualize the umbrella clause standard from the

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<sup>41</sup> Australia-Poland Bilateral Investment Treaty (1991) art 10.

<sup>42</sup> K Yannaca-Small, 'Interpretation of the Umbrella Clause in Investment Agreements' [2006] *OECD Working Papers on International Investment* 10.

<sup>43</sup> WTO Doc WT/WGTI/W/122 (27 June 2002), cited in Surya P Subedi, *International Investment Law: Reconciling Policy and Principle* (Hart 2008) 183.

perspectives of the host developing countries. The awards given by the arbitral tribunals have a lack of consistency and sometimes same issue has been decided on the contrary manner. Because foreign investors frequently invoke the umbrella clause against host developing nations, arbitral tribunals varied and imprecise interpretations of the clause expose host developing countries to significant risk and high expenses. The actions taken by the developing countries in case of necessity in a crisis is a well-established principle in international law. For any choice to preserve the country and the public interest, developing countries are at the mercy of arbitral tribunals.

The majority of the tribunals broaden the scope of the umbrella clause and put pressure on the developing states by not considering the challenges developing countries face such as social and political instability, economic crisis, lack of resources, and limited administrative capacity. However, these problems should be considered when the tribunals assess the obligations of the country. Otherwise, discrimination will always increase between investors and developing countries.

**(b) Scope of building equitable relationships keeping in mind the conditions of the developing countries:**

As seen in the preceding part, confusion has been raised among the developing states because of pointing different directions and inconsistent decisions by the arbitral tribunals regarding the characteristics of the umbrella clause. This paper aims to explore different ways and means of addressing the current challenges faced by the developing countries for the BITs are being signed by them as their perspectives are not considered in the BITs or by the arbitral tribunals.

However, it is possible to build a non-discriminatory and equitable relationship between the developed countries and the developing countries, if the security of the investors can be given and the conditions of the developing countries can be considered when the investment treaties are being signed and also when the disputes are in the hand of the tribunals.

**New Strategies Needed: Need to have a Global Model BIT to Reduce Discrimination**

It is clear that the developed countries are mainly the investor and the developing countries are the host countries in most of the cases dealt with by the arbitral tribunals. Though there may be some BITs among the developed countries. In recent years some of the other countries are making their model BIT for the convenience of making foreign investment. As the developing countries need development and for attracting developed countries investors', they try to offer every kind of benefit for them without considering the side effects. The investors also do not care about the development or anything about the host country but profits. This may be helpful for both the investors and the host countries. However, it does not create a fair and equitable relationship between the countries, and there creates huge discrimination in law treating the countries when any conflict is raised. If it continues, it will have a

great impact on international investment law. It is indeed a time to have a regulation or model treaty for general obligations for the investors and the host countries to ensure proper protection of the investors and their property as well as proper security for the developing or least developed country from the arbitrary actions of the investors.

The arbitral tribunals in several cases have gone beyond the established principle of international law to decide different BIT disputes. There is no clear guidance on characteristics of the umbrella clause with other provisions of the BIT and also no obligations for the investors for breaches of obligation. As there are no global treaty and precedent to follow by tribunals, tribunals give controversial explanations on the same issue. There is no internationally recognized definition of different principles the and umbrella clause is one of the most controversial among them. So, it creates a problem.

However, the experience in this regard is not so good as the attempt of the OECD in the 1990s to conclude a Multilateral Investment Agreement (MAI) failed. The Doha Declaration was also set aside by the WTO. There are also different model BITs written by different developed countries which they follow when they make any BIT with other countries. There is a model BIT among the ASEAN countries which they follow when signing BIT between the ASEAN countries. Many individual countries like Germany have their model BIT which they follow when they make a treaty with other countries. Point to be noted that there are few model BITs written by any developing country.

There are more than 2500 BITs in the present time and they mostly hold similar provisions with some differences. It is indeed a great time to build a consensus among the countries to have a specified umbrella clause and its characteristics will be clear for the investors and the host developing countries. As having a binding treaty in the first instance is not so easy and the experience is bitter in this regard, making a model BIT can be appropriate guidance for making the future BITs among the countries. To fulfill this purpose, the WTO can play a great role.

According to the classification of the UN regarding the developed and developing states, there are more developing states in the world. the policymakers of the developing countries should come forward for having balance BITs with the investors. The policymakers of these countries may have an agreement on dealing with the investment agreement by protecting their interests and having a balance in the relationship with the investors. Otherwise, the unusual discriminatory relationship with investors and the huge burden will make their countries more vulnerable as well as the local companies will also be discriminated from the state policy which will make them indifferent to investing in their own country.

The WTO is the highest forum for international trade. So, the united policymakers of the developing countries may approach the authority for having a global model BIT. there may have a big discussion among the policymakers. Both Parties will be able to make clear their argument and a great model BIT may establish. As a result, the

future BITs will be more balanced and the investors or the host states can't impose arbitrary provisions for more security, the model BIT will work as a guide for the BITs. As regards the umbrella clause, the useful language for both investors and the host countries will increase the credibility of the clause and the tribunals will also be reasonable in interpreting the clause.

If an international model BIT is made, the concerned parties especially the developing countries would be able to contribute to the making of the general provisions of the treaty which will reflect their perspective also. On the other hand, a model BIT may ensure the protection of the investors by ensuring a uniform and consistent form of umbrella clause considering the perspective of the concerned countries as well as harmonizing different rules, trends, and practices on this. This will lessen the need for having BITs in different forms and languages between countries. Especially, the umbrella clause and its characteristics will be clear for all and it will be non-discriminatory.

#### Revision of Existing BITs:

It is seen that many new BITs skipped the umbrella clause in their BIT for its ambiguous and discriminatory nature. If the developed and developing countries can build a consensus to harmonize the scope and characteristics of the umbrella clause through model BIT and practice, the investors and the host countries can revise the BITs signed among them. The investors generally have basic knowledge regarding the conditions of the specific countries they are investing and knowing the situations there they agreed to sign the BIT. So, reasonable risks should be taken by the investors. As a result, the existing BITs between the developed and developing countries should be revised based on the model BIT.

A BIT generally becomes effective for decades between the investors and the host states, so in this 21<sup>st</sup> century to save countries from discrimination and huge risk the existing BITs need to be revised considering the updated model BIT.

The investment treaties could extend the requirement to consider that the investors shall ensure the environmental, human rights, and other social and political impacts in the host country concerned. There should have access for the victims of the host countries to international courts and tribunals where the activities of the foreign investors grossly undermine human rights and the environment. In this era, the human rights issue and the environmental issue are indeed getting great priority but there is no international legal framework or effective remedy for the victims before international courts and tribunals against the perpetrators of such violations.

#### **Interpretive statements by the International Law Commission on Umbrella Clause**

As the ILC was entrusted to draft articles on State Responsibility in 2001 or articles on MFN clauses in 1978, the ILC can also be entrusted to formulate the interpretation of the umbrella clause. A number of factors could be taken into account from the perspective of both developed and developing countries to define

the meaning, nature and scope of the umbrella clause. In case of the interpretation of the umbrella clause by any authority such as arbitral tribunals, the interpretation of the ILC would have a significant weight. If this is incorporated into the international instrument, especially in the BITs this would go a long way in guiding the international investment tribunals. The umbrella clause should be rethought from the perspective of developing countries, taking into account their developmental concerns and challenges, in order for arbitral tribunals to take consistent and acceptable methods. The predictability of the clause's reach would have a significant impact on these countries' capacity to attract foreign investment.

### **Using of Host States' Court for Resolving Investment Dispute:**

It is correct that the reasons for using the umbrella clause in the investment treaties are not getting fair justice in the host state local courts as mostly, they are influenced by the government of the country and the judiciary is not independent in most of the countries. However, if a model treaty is established with the consensus of the countries of developed and developed countries, the policymakers can propose a neutral judicial body in the host states for resolving the investment disputes without any interference from the local government primarily. If the court of the host state becomes biased and does not ensure fair and non-biased decisions and does not follow due process of law, the investors will have the right to go to the international arbitral tribunal for a final decision on the investment disputes. As a result, the huge cost of the developing country to become party to the international arbitral tribunal's case will be saved as well as the investors will also be able to get justice easily without much cost. Though the developed country may feel insecure like before the international law is more established than before and all the nations can easily know the facts and circumstances of any country in the world. As a result, if any developing country does not follow due process of law in resolving investment disputes, it will be known by all the investors of the world and later they will have the option to decide not to invest in the specific host developing country. If the trust can be established among the investor, the huge cost will also be saved and a legal and fair decision will be able to get by the parties more easily than in the present time as there will be an explanation of the term umbrella clause by the international law commission.

### **7. Conclusion**

Historically, the umbrella clause is incorporated in the bilateral investment treaties for the protection of the investors in the host countries. There was nothing considering the conditions of the developing countries. However, the scope of the umbrella clause increased its favor for the investors from time to time without any specific guidelines and created ambiguities in the mind of the policymakers of the developing countries. There is no way to accept the imposed obligations through the umbrella clauses in the bilateral investment treaties by the developed countries as foreign investment is necessary for the development of the developing countries.

However, the conflicting decisions of the arbitral tribunals make the clause ambiguous and the tribunals do not consider the economic, social, political, and other difficulties faced by the developing countries when they are dealing with any investment dispute. The umbrella clause is discriminatory and builds inequitable relationships between the investors and the host state as well as local investors trying to invest in other countries rather than in their own country as more security is ensured by the umbrella clause. The umbrella clause creates an imbalance in the arena of investment law.

There is an emergency need to consider the conditions of the developing countries along with the security of the investors to make the relationship between the investors and the host states equitable otherwise this discriminatory approach of the umbrella clause would make the relationship more imbalanced. This paper suggests that the developing states could be proposed to consider their perspective in bilateral investment treaty by having an international model BIT where the umbrella clause will try to be equitable for both the investors and the developing states. For specific guidelines, the ILC can be entrusted to give interpretative statements regarding the characteristics of the umbrella clause, and later the revisiting of the existing can be one of the effective ways to make the equitable relationship between the investors and the developing states. Lastly, the host states' court can be entrusted to resolve investment disputes primarily with conditions and if it fails then the international tribunal will decide the case.

This paper mainly focused on perspective of the umbrella clause as the use of the umbrella clause increased vastly in the last few decades, this paper would show the policymakers of the developing countries that there is possibility of having through different manners as mentioned here. Four and to get make a balance relationship in the investment treaty the policymakers of the developing countries should be united and raised their voice in the international forum such as WTO for making a model BIT and taking other possible actions such as explanation of the umbrella clause as well as other principles related to the investment treaty through ILC and having a clear and specific guideline regarding the dispute settlement forum and principles. Lastly, they can be agreed to ensure protection of the investors and ensure due process of law when national court would try to resolve any dispute.

There have been few research specifically considering the perspective of the developing countries regarding the characteristics of umbrella clause and also characteristics of other principle. The future researchers work trying to be more specific regarding proper language of the umbrella clause as it has huge impact on the decision of the tribunals as well as the possibility of having any new binding treaty balancing the relationship between the investors and the developing states.