Journal of Arbitration Studies, Vol. 23 No. 3
September, 2013, pp. 127~147

Received : August, 12, 2013
Revised : August, 23, 2013
Accepted : August, 25, 2013

The Protection Offered by "Umbrella Clauses"in Korean Investment Treaties*

Caline Mouawad**
Elodie Dulac***

Korea is, after China, the Asian country with the largest number of concluded investment treaties. One of the protections that Korean investment treaties frequently afford to foreign investors and their investment is the so?called "umbrella clause," which requires the host state of the investment to observe the commitments that it has undertaken toward the foreign investor or its investment. This is a potentially very powerful protection. Umbrella clauses, however, have proven to be amongst the most controversial provisions in investment treaties, giving rise to diverging interpretations by tribunals and commentators that are still not reconciled today.

Key Words : Investment Treaty, Free Trade Agreement, Umbrella Clause, Most Favoured Nation Clause, MFN Clause

< Contents >

* The views in this article are personal to the authors and do not necessarily represent the views of King & Spalding or its clients.

** A Partner in King & Spalding's International Arbitration Practice Group, based in the firm's New York office, U.S.A.

*** A Senior Associate in King & Spalding's International Arbitration Practice Group, based in the firm's Singapore office, Singapore

I. Introduction

Under investment treaties, states undertake to promote and protect investments made by the investors of the other contracting state(s) in their territory. A distinctive feature of investment treaties—and treaties entered into by the Republic of Korea ("Korea") are no exception—is that they almost systematically give foreign investors the means to enforce these protections by commencing an international arbitration against the host state of their investment.

Investment treaties typically offer a number of protections to foreign investors and their investment, such as fair and equitable treatment of the investment, protection against unlawful expropriation, as well as—and this is the focus of this article—the so-called "umbrella clause," also known as an "observance of undertakings" clause. Korean investment treaties frequently contain an umbrella clause. In a nutshell, an umbrella clause is a provision that requires the host state of the investment to observe the commitments that it has undertaken toward the foreign investor or its investment. This is a potentially very powerful protection, on which foreign investors have relied to bring claims before investment treaty arbitral tribunals for breach by the host state of a contract with the investor (*e.g.*, a concession agreement).[1] Umbrella clauses, however, have proven to be amongst the most controversial provisions in investment treaties,

1) On umbrella clauses, see, *e.g.*, Christoph H. Schreuer, "Travelling the BIT Route - Of Waiting Periods, Umbrella Clauses and Forks in the Road", Journal of World Investment & Trade, vol. 5, no. 2, April 2004, pp.231 et seq.; Stanimir A. Alexandrov, "Breaches of Contracts and Breaches of Treaty - The Jurisdiction of Treaty-Based Arbitration Tribunals to Decide Breach of Contract Claims in SGS v. Pakistan and SGS v. Philippines," Journal of World Investment & Trade, Vol.5 No.4, August 2004, pp. 555 *et seq.*; Emmanuel Gaillard, "Investment Treaty Arbitration and Jurisdiction over Contractual Claims - The SGS v. Pakistan and SGS v. Philippines precedents," in T. Weiler (ed), *International Investment Law and Arbitration - Leading Cases from the ICSID, NAFTA, Bilateral Investment Treaties and Customary International Law,* Cameron May, 2005; T.G. Weiler (ed.), "Part I - Umbrella Clause," in *Investment Treaty Arbitration and International Law,* JurisNet, 2008; OECD, "The Interpretation of the Umbrella Clause in Investment Agreements," Working Papers on International Investment, No 2006/3, October 2006; Rudolf Dolzer and Christoph Schreuer, *Principles of International Investment Law,* Oxford University Press, 2nd ed., 2012, pp. 166 et seq.; and Abby Cohen Smutny and Steven Lee, "Chapter 15 The MFN Clause: What Are Its Limits," in Katia Yannaca-Small, *Arbitration Under International Investment Agreements - A Guide to the Key Issues,* Oxford University Press, 2010.

giving rise to diverging interpretations by tribunals and commentators that are still not reconciled today.

In this article, we will survey Korea's investment treaty programme and umbrella clauses found in Korean investment treaties (II). We will then turn to the interpretation of umbrella clauses and their effect (III). Lastly, we will consider the use of a most-favoured-nation clause to import an umbrella clause in Korean investment treaties which do not contain one, thereby enhancing investment protection (IV).

II. Korean Investment Treaties and Umbrella Clauses

A. Overview of Korea's Investment Treaty Programme

There are today over 2,600 bilateral investment treaties ("BITs"). There is also a growing number of free trade agreements ("FTAs") containing an investment protection chapter, which are similar to BITs in their content. In this article, we refer to BITs and FTAs as "investment treaties."

Korea is, after China, the Asian country with the largest number of investment treaties. It is also one of the top ten countries in terms of number of concluded BITs. At the time of writing, Korea is a party to 90 BITs, 82 of which are in force.[2)]

Korea's first BIT, with Germany, dates back to 1964. In the 1970s and 1980s, Korea entered into few investment treaties, mostly with developed countries in Europe. Most investment treaties concluded by Korea since the mid-1990s are with developing countries, reflecting Korea's growing role as a source of outbound investment.

The latest wave of Korean investment treaties dates from 2006-2007. Since 2007, although it has entered into only one BIT—with Uruguay—Korea has entered into a number of FTAs containing an investment chapter, *e.g.*, a 2009

2) *See* the list of Korean BITs and the text of most of them at <http://www.unctadxi.org/templates/DocSearch____779.aspx> (last visit on July 29, 2013).

Agreement on Investment with ASEAN member states, a 2009 FTA with the United States, a 2009 FTA with India, and a 2011 FTA with Peru.[3)]

Korea signed a tripartite investment agreement with China and Japan to replace the three existing investment treaties between these countries.[4)] It is also negotiating investment treaties with Australia-New Zealand, Canada, and Mexico.

To date, there has been only one reported investment arbitration case under a Korean investment treaty. It is a case brought against Korea by a U.S. private equity fund, Lone Star Funds, under the Belgium/Luxembourg-Korea BIT in relation to its investment in the financial institution Korea Exchange Bank. The case is ongoing.[5)]

B. Umbrella Clauses in Korean Investment Treaties

Of the Korean investment treaties publically available, a majority contain an umbrella clause, and almost all of the Korean investment treaties concluded between 1995 and 2006 do. Korea seems to have abandoned umbrella clauses in its recent FTAs (for example, its FTA with the United States does not contain one).

While umbrella clauses are a well-known provision in investment treaties, such a frequent inclusion is unusual. As an illustration, taking China, the other Asian country in the top ten countries in terms of the number of concluded BITs, only approximately a third of Chinese investment treaties contain an umbrella clause.

The most common wording of umbrella clauses encountered in Korean investment treaties is as follows:

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

3) *See* the list and text of Korean FTAs at <http://www.mofat.go.kr> and <http://aric.adb.org/FTAbyCountryAll.php> (last visit on July 29, 2013).

4) *See* Agreement among the Government of Japan, the Government of the Republic of Korea and the Government of the People's Republic of China for the Promotion, Facilitation and Protection of Investment (signed on May 13, 2012; ratification pending).

5) *See* "Lone Star Claims Against South Korea Has An Arbitral Tribunal in Place," Investment Arbitration Reporter, May 13, 2013, available at <http://www.iareporter.com/articles/20130513> (last visit on July 29, 2013).

Party."[6]

The only noticeable evolution in the drafting of umbrella clauses in Korean investment treaties concerns the location of the umbrella clause in the treaty. Until 1992, the umbrella clause was located at the beginning of the treaty, among the provisions extending substantive treatment protections to investments and investors. From 1992 onwards, the umbrella clause usually is found at the end of the treaty, after the treatment provisions and after the dispute resolution provisions, in an article entitled "application of other rules" (or similar title).[7] We will discuss in Section IV below what impact, if any, the location of the umbrella clause in the treaty may have on its interpretation.

Based on publically available BITs, Korea's BITs with the following (nearly 50) countries contain an umbrella clause: Albania, Algeria, Bangladesh, Belarus, Bolivia, Brazil, Brunei Darussalam, Burkina Faso, Cambodia, Costa Rica, Croatia, Democratic Republic of Congo, Denmark, El Salvador, Greece, Guatemala, Honduras, Iceland/Lichtenstein/Switzerland, Jamaica, Hong Kong, Jordan, Kazakhstan, Kuwait, Laos, Latvia, Lebanon, Mauritania, Morocco, Nicaragua, Nigeria, Oman, Pakistan, Panama, Paraguay, Portugal, Qatar, Romania, Russia, Saudi Arabia, South Africa, Tajikistan, Tanzania, Thailand, Trinidad and Tobago, Turkey, Ukraine, United Kingdom, Uzbekistan.[8]

III. The Effect of Umbrella Clauses in Korean Investment Treaties

The effect of umbrella clauses is one of the most unsettled issues in investment treaty jurisprudence. A consensus seems to have emerged that umbrella clauses may have the effect of elevating into treaty breaches violations by the host state of the commitments that it has undertaken towards the foreign investor or its investment, be it in a contract or in unilateral undertakings such

6) Article 2(2) of the Korea-United Kingdom BIT.
7) See the text of these BITs at <http://www.unctadxi.org/templates/DocSearch____779.aspx> (last visit on July 29, 2013).
8) *Id.*

as legislation (A). However, the controversy lies in the details as to when an umbrella clause may have such an effect (B).

A. The "Elevating Effect" of Umbrella Clauses Is Accepted in Principle

According to the now prevailing interpretation, an umbrella clause would have the effect of elevating any breach of a commitment undertaken by the host state with regard to the investment or the investor—whether in a contract or in legislation—into a breach of the treaty, which could be submitted by the investor to an investment treaty tribunal. In the words of the tribunal in the *LESI Dipenta v. Algeria case, "the effect of such clauses is to transform the violations of the State's contractual commitments into violations of the treaty umbrella clause and by this to give rise to jurisdiction of the Tribunal over the matter."*[9] This interpretation is also the one favoured by a majority of commentators.[10]

---

9) *Consortium Groupement L.E.S.I.- DIPENTA v. République algérienne démocratique et populaire,* ICSID Case No. ARB/03/08, Award dated January 10, 2005, 25. *See also, e.g., SGS Société Générale de Surveillance S.A. v. Republic of the Philippines,* ICSID Case No. ARB/02/6, Decision of the Tribunal on Objections to Jurisdiction dated January 29, 2004 (*"SGS v. Philippines"*), 134 *et seq.; Eureko BV v. Republic of Poland,* Partial Award dated August 19, 2005 (*"Eureko v. Poland"*), 257 *et seq.*; *Noble Ventures, Inc v. Romania,* ICSID Case No. ARB/01/11, Award dated October 12, 2005 (*"Noble Ventures v. Romania"*), 51 *et seq.; Bureau Veritas, Inspection, Valuation, Assessment and Control, BIVAC B.V. v. The Republic of Paraguay,* ICSID Case No. ARB/07/9, Decision of the Tribunal on Objections to Jurisdiction dated May 29, 2009 *("BIVAC v. Paraguay")*, 141 ("the conclusion has prevailed that [the umbrella clause] of the BIT establishes an international obligation for the parties to the BIT to observe contractual obligation with respect to investors"); *SGS Société Générale de Surveillance S.A. v. The Republic of Paraguay,* ICSID Case No. ARB/07/29 (*"SGS v. Paraguay"*), Decision on Jurisdiction dated February 12, 2010, 162 et seq., and Award dated February 10, 2012, 89 et seq.

10) *See, e.g.,* Emmanuel Gaillard, *La Jurisprudence du CIRDI,* Pedone, 2004, pp.759 *et seq.* and pp.833-835; Christoph H. Schreuer, "Travelling the BIT Route - Of Waiting Periods, Umbrella Clauses and Forks in the Road," Journal of World Investment &Trade, Vol.5 No.2, April 2004, pp.231 *et seq.*; Stanimir A. Alexandrov, "Breaches of Contracts and Breaches of Treaty - The Jurisdiction of Treaty-Based Arbitration Tribunals to Decide Breach of Contract Claims in SGS v. Pakistan and SGS v. Philippines," Journal of World Investment & Trade, Vol.5 No.4, August 2004, pp.555 *et seq.*; T.G. Weiler (ed.), "Part I - Umbrella Clause," in *Investment Treaty Arbitration and International Law,* JurisNet, 2008; and OECD, "The Interpretation of the Umbrella Clause in Investment Agreements," Working Papers on International Investment, No 2006/3, October 2006.

As an illustration, in the *Eureko v. Poland* case, the tribunal held that Poland's violation of contractual undertakings relating to the privatisation of its leading insurance group gave rise to a breach of the umbrella clause contained in the Netherlands-Poland BIT.[11] More recently, in EDFI v. Argentina, the tribunal held Argentina liable for breach of the umbrella clause of the Argentina-France BIT resulting from Argentina's repudiation of its obligations under an electricity concession agreement entered into with the claimants.[12] As another illustration, in *SGS v. Paraguay,* the tribunal held that Paraguay had breached the umbrella clause of the Swiss-Paraguay BIT by failing to pay for services under a contract to inspect goods that it had concluded with SGS. Paraguay was ordered to pay SGS compensation in an amount over USD 57 million.[13]

To reach such conclusions, tribunals have focused on the broad wording of the umbrella clause before them, which referred to "any obligation" and imposed a mandatory obligation by its terms "shall observe."[14] Such wording is similar to that of umbrella clauses in Korean BITs, which therefore should have the same elevating effect in accordance with the prevailing interpretation.

It should be mentioned that the first tribunal called upon to interpret an umbrella clause in the early 2000s—the *SGS v. Pakistan* tribunal—rejected the elevating effect of umbrella clauses, without however ascribing any alternative meaning to that clause. This decision was widely criticised, both by commentators and subsequent tribunals, as effectively depriving the umbrella clause of any effect.[15] It remains an isolated decision.

As mentioned in Section III above, the main evolution in the umbrella clauses contained in Korean investment treaties over time has been their location, from being included in the treatment provisions to being moved towards the end of the treaties in an "application of other rules," or otherwise similar, provision.

---

11) *See Eureko v. Poland,* 244 *et seq.*

12) *See EDF International S.A., SAUR International S.A. and León Participaciones Argentinas S.A. v. Argentine Republic,* ICSID Case No. ARB/03/23, Award dated June 11, 2012, 938 et seq.

13) *See SGS v. Paraguay,* Award dated February 10, 2012, 162 *et seq.*

14) *See SGS v. Philippines,* 15.

15) *See, e.g., SGS v. Philippines,* 119 *et seq.; SGS v. Paraguay,* Decision on Jurisdiction dated February 12, 2010, 169; and Emmanuel Gaillard, *La jurisprudence du CIRDI,* Pédone, 2004, p.834.

With very rare exceptions, tribunals have not considered the location of umbrella clauses as determinative of whether they should have an elevating effect.[16] The change of the location of umbrella clauses in Korean investment treaties therefore should have no bearing on their elevating effect.

The above examples related to a state's contractual undertakings. Going further, a number of arbitral tribunals have held that unilateral undertakings given by the host state to foreign investors in legislation (and not only contractual commitments) also could give rise to a breach of an umbrella clause. For example, the LG&E v. Argentina tribunal considered that the Argentine Gas Law and implementing regulations were specific obligations undertaken by Argentina towards foreign investors, including the claimant, and that these *"became obligations ... that gave rise to liability under the umbrella clause"* of the Argentina-United States BIT. *The LG&E v. Argentina* tribunal concluded that Argentina's changes to its Gas Law and implementing regulations constituted a breach of the umbrella clause.[17]

As in any matters under investment treaties, however, the text of the particular treaty applicable should be examined, as it may contain restrictive language. For instance, some investment treaties expressly refer to "contractual" commitments in their umbrella clauses.[18] This type of wording in all likelihood would limit umbrella clauses claims to breaches of contractual commitments, to the exclusion of commitments given by the host state in legislation or otherwise. To our knowledge, no Korean investment treaty contains an umbrella clause expressly referring to "contractual" commitments.

This being said, the vast majority of umbrella clauses in Korean investment treaties contain the wording "obligation [the host state] may have entered into with regard to investments of nationals or companies of the other Contracting

16) *See SGS v. Pakistan,* 169-170; and *Joy Mining Machinery Limited v. The Arab Republic of Egypt,* ICSID Case No. ARB/03/11, Award on Jurisdiction dated August 6, 2004, 81.

17) *See LG&E Energy Corp. et al. v. Argentine Republic,* ICSID ARB/02/1, Award dated July 25, 2007, 170 *et seq.; and SGS v. Paraguay,* Decision on Jurisdiction dated February 12, 2010, 167.

18) *See, e.g.,* Article 9 of the China-Jordan BIT ("[e]ach Contracting Party shall observe any contractual obligation it may have entered into towards an investor with regard to investment approved by it in investment treaties territory.").

Party" (emphasis added). Some tribunals have found that the phrase "entered into" limits the scope of the umbrella clause to contractual obligations, to the exclusion of general obligations arising from the law of the host state. In the words of the Noble Ventures v. Romania tribunal:

> *"The employment of the notion 'entered into' indicates that specific commitments are referred to and not general commitments, for example by way of legislative acts."* [19]

However, as an illustration of the divide in the jurisprudence on umbrella clauses, at least one other tribunal, in *Liman Caspian Oil v. Kazakhstan,* reached the opposite conclusion and found that an umbrella clause containing the phrase "entered into" could cover legislative promises.[20] In view of the inconsistent decisions on this point, investors under Korean investment treaties at least should be mindful that they may have more difficulty bringing an umbrella clause claim for breach by the host state of a commitment arising out of legislation than for breach of a contract with the host state.

While arbitral tribunals have almost invariably accepted that an umbrella clause in principle could have an elevating effect—notably to elevate a contractual breach into a treaty breach—the circumstances in which it will have such effect have given rise to controversy and divergent decisions on a number of sub-issues. These include the impact of a forum selection clause in the underlying contract, whether sovereign conduct is required to trigger a breach of the umbrella clause, and the identity of the parties to the underlying contract for that contract to fall within the scope of the umbrella clause. We examine these issues below.

---

19) *See Noble Ventures v. Romania,* 51. *See also Mohammad Ammar- Al-Bahloul v. Tajikistan,* SCC Case No. V(064/2008), Partial Award on Jurisdiction and Liability dated June 18, 2010 (*"Al-Bahloul v. Tajikistan"*), 257, with reference to the umbrella clause at Article 10(1) of the Energy Charter Treaty ("In both cases, however, it is clear that the obligation must have been entered into 'with' an Investor or an Investment of an Investor. Therefore, this provision does not refer to general obligations of the State arising as a matter of law.").

20) *See Liman Caspian Oil BV and NCL Dutch Investment BV v. Republic of Kazkhstan,* ICSID Case No. ARB/07/14, Award dated June 22, 2010 (*"Liman Caspian Oil v. Kazakhstan)*, 448.

B. Thorny Issues Relating to the Effect of Umbrella Clauses

(1) What Is the Impact of a Forum Selection Clause in the Underlying Contract on an Umbrella Clause Claim?[21]

In cases where a foreign investor seeks to elevate a breach of contract by the host state into a breach of an investment treaty, the underlying contract may contain its own dispute settlement provision, such as an exclusive forum selection clause designating domestic courts or providing for arbitration under the contract.

Investment treaty tribunals have held most consistently that contractual forum selection clauses do not bar investors from bringing claims in relation to contracts on the basis of investment treaties. In other words, investment treaty tribunals have distinguished between the causes of action—"contractual claims" and "treaty claims"—and have retained jurisdiction over the latter, notwithstanding the existence of a contractual dispute resolution clause.[22]

The question is slightly more delicate regarding umbrella clauses, as their breach is premised upon finding that the host state breached a contractual commitment in the first place (where contractual commitments, and not legislation, by the host state are at stake).

To our knowledge, no tribunal has ever denied jurisdiction over an umbrella clause claim based on the existence of a forum selection clause in the underlying contract. In two cases, arbitral tribunals have held that they had jurisdiction but refused to exercise it: they stayed the proceedings and referred the parties to the contractual dispute resolution mechanism.[23] In all other

---

21) This section is solely concerned with umbrella clauses. It does not address the separate situation where an investor has an investment agreement with the host state and the investor-state dispute resolution provision of the applicable investment treaty provides for the investment treaty tribunal's jurisdiction over investment agreements.

22) See, e.g., the landmark case, *Compañiá de Aguas del Aconquija S.A. and Universal v. Argentine Republic*, ICSID Case No. ARB/97/3, Decision on Annulment dated July 3, 2002.

23) *See SGS v. Philippines,* 127-128, where the tribunal, while recognising for the first time the elevating effect of an umbrella clause, stayed the arbitration, and referred the parties to the contractual forum selection clause—which designated Philippine courts—for a determination of the scope or extent of the host state's contractual obligations (or alternatively, giving the

umbrella clause cases, *i.e.*, the majority of them, arbitral tribunals have retained and exercised jurisdiction over claims for breach of an umbrella clause, notwithstanding the existence of a forum selection clause in the underlying contract.[24] In doing so, the *SGS v. Paraguay* tribunal stressed that *"[a]t least in the absence of express waiver, a contractual forum selection clause should not be permitted to override the jurisdiction to hear Treaty claims [i.e. an umbrella clause claim] of a tribunal constituted under that Treaty."*[25]

(2) Is Sovereign Conduct Necessary to a Finding of Breach of an Umbrella Clause?

A number of tribunals have introduced a distinction, derived from international law on state immunities, between the host state acting as a sovereign and as an ordinary contractual party. According to this approach, umbrella clauses would cover only contracts entered into by the state as a sovereign (as opposed to a commercial contract),[26] or breached by the host state acting in a sovereign capacity (as opposed to an ordinary contractual party).[27]

Such restriction to the full effect of umbrella clauses, which is not found in

---

parties the option to agree among themselves on this point, which they eventually did and the stay was lifted. The case settled shortly after the lift of the stay). For a more recent decision, see *BIVAC v. Paraguay,* 143 *et seq.,* in which the tribunal stayed the proceedings and referred the parties to the exclusive forum selection clause in the underlying contract. *See also the obiter dicta in Bosh International, Inc. et al. v. Ukraine,* ICSID Case No. ARB/08/11, Award dated October 25, 2012 (*"Bosh v. Ukraine"*), 252 *et seq.* For a criticism of the stay of proceedings in the above two cases, *see* Emmanuel Gaillard, "Investment Treaty Arbitration and Jurisdiction over Contractual Claims – The SGS v. Pakistan and SGS v. Philippines precedents," in T. Weiler (ed), *International Investment Law and Arbitration – Leading Cases from the ICSID, NAFTA, Bilateral Investment Treaties and Customary International Law,* Cameron May, 2005, p.334.

24) *See, e.g., SGS v. Paraguay,* Decision on Jurisdiction dated February 12, 2010, 172 *et seq.*

25) *Id.*, 180.

26) *See El Paso Energy International Company v. The Argentine Republic,* ICSID Case No. ARB/03/15, Decision on Jurisdiction dated April 27, 2006, 79 *et seq.*; and *Pan American Energy LLC and BP Argentina Exploration Company v. Argentine Republic,* ICSID Case No. ARB/03/13 and *BP America Production Co. and Others v. Argentine Republic,* ICSID Case No. ARB/04/8, Decision on Preliminary Objections dated July 27, 2006, 108 et seq.

27) *See, e.g., Sempra Energy International v. The Argentine Republic,* ICSID Case No. ARB/02/16, Award dated September 28, 2007 (*"Sempra v. Argentina"*), 310 *et seq.*

the text of the applicable investment treaties, has been criticised harshly by commentators and has been rejected, implicitly or explicitly, by a majority of arbitral tribunals.[28] One recent explicit rejection came from the tribunal in *SGS v. Paraguay,* which held that:

> *"Given the unqualified nature of Article 11 of the Treaty [i.e. the umbrella clause, which had a wording similar to the ones of Korean BITs], and its ordinary meaning, we see no basis to import into Article 11 the non-textual limitations that Respondent proposed in its Reply. Article 11 does not exclude commercial contracts of the State from its scope. Likewise, Article 11 does not state that its constant guarantee of observance of such commitments may be breached only through actions that a commercial counterparty cannot take, through abuse of state power, or through exertions of undue government influence… In effect, we see no basis on the face of the clause to believe that it should mean anything other than what it says – that the State is obliged to guarantee the observance of its commitments with respect to the investments of the other State party's investors."*[29]

28) *See, e.g.,* Emmanuel Gaillard, "A Black Year for ICSID," New York Law Journal, March 1, 2007. *See also Duke Energy Electroquil Partners & Electroquil S.A. v. Republic of Ecuador,* ICSID Case No. ARB/04/19, Award dated August 18, 2008, 320; and *Burlington Resources Inc. v. Republic of Ecuador,* ICSID Case No. ARB/08/5, Decision on Jurisdiction dated June 2, 2010, 190, for a rejection of the distinction sovereign/commercial as regards umbrella clauses.

29) *SGS v. Paraguay,* Decision on Jurisdiction dated February 12, 2010, 168, and Award dated February 10, 2012, 91 et seq. (In short, if Paraguay failed to observe its contractual commitments, then it breached Article 11 [*i.e.*, the umbrella clause]. No further examination of whether Paraguay's actions are properly characterized as 'sovereign' or 'commercial' in nature is necessary.").

3. Who Should Be Party to the Underlying Contract for the Contract to Fall Within the Scope of an Umbrella Clause?

Where an umbrella clause claim is based on an alleged breach of a contractual commitment by the host state, the identity of the parties to the underlying contract may be relevant to an arbitral tribunal's analysis of whether the umbrella clause is applicable.[30] It may be that the investor bringing the claim is not a party to the underlying contract, for instance because its locally-incorporated subsidiary is. Or it may be that the host state itself is arguably not a party to the underlying contract, for instance because a state-owned enterprise or another entity which under municipal law has a legal personality distinct from the state is. Arbitral decisions to date do not offer a consistent answer as to which entities should be party to the underlying contract for it to be covered by an umbrella clause.

With regard to the party to the underlying contract on the investor's side, some arbitral tribunals have held that a contract to which the foreign investor itself is not a party—for instance, where a locally-incorporated subsidiary entered into the contract—is not covered by the umbrella clause.[31]

Conversely, other tribunals have accepted that umbrella clauses cover a contract entered into by the foreign investor's subsidiary.[32] As an illustration, in

---

30) *See* Nick Gallus, "An Umbrella Just for Two? BIT Obligations Observance Clauses and the Parties to a Contract," Arbitration International, Vol.24 No.1, 2008, pp. 157 *et seq.*

31) *See Azurix v. Argentine Republic,* ICSID Case No. ARB/01/12, Award dated July 14, 2006 (*"Azurix v. Argentina"*), 384; *Siemens A.G. v. Argentina,* ICSID Case No. ARB/02/08, Award dated February 6, 2007, 204; *CMS Gas Transmission Company v. The Republic of Argentina,* ICSID Case No. ARB/01/8, Decision of the Ad Hoc Committee on the Application for Annulment dated September 25,2007, 95; *Burlington Resources Inc. v. Republic of Ecuador,* ICSID Case No. ARB/08/5, Decision on Liability dated December 14, 2012, 212 *et seq.*; and *Liman Caspian Oil v. Kazakhstan,* 443.

32) *See CMS Gas Transmission Company v. The Republic of Argentina,* ICSID Case No. ARB/01/8, Award dated May 12, 2005, 296 et seq.; *Enron Corporation and Ponderosa Assets, L.P. v. Argentine Republic,* ICSID Case No. ARB/01/3, Award dated May 22, 2007, 269 *et seq.; Sempra v. Argentina,* 308 et seq.; and *Limited Liability Company Amto v. Ukraine,* SCC Case No. 080/2005, Final Award dated March 26, 2008 (*"AMTO v. Ukraine"*), 110.

Continental Casualty v. Argentina, the tribunal held in its discussion of the umbrella clause claim that, *"provided that these obligations have been entered into 'with regard' to investments, they may have been entered with persons or entities other than foreign investors themselves, so that an undertaking by the host State with a subsidiary… is not in principle excluded."*[33]

In light of this divided jurisprudence, what can be said at this stage is that the specific wording of the umbrella clause in the applicable treaty may be a relevant consideration. Some tribunals have made a distinction depending on whether the umbrella clause referred to commitments "entered into with regard to *investments*"— which would cover a contract between the investor's locally-incorporated subsidiary and the host state—or to "commitments entered into with the investors"—which would only cover contracts between the investor itself and the host state.[34] Umbrella clauses in Korean investment treaties contain the wording "with regard [or "with respect"] to investments," and accordingly would appear to allow for the former interpretation.

With regard to the party to the underlying contract on the host state's side, and contracts entered into by sub-state entities (*e.g.,* a province of the host state, state agency or a state-owned company), arbitral decisions are equally divided. Some arbitral tribunals have applied the international law rules on attribution, and have upheld jurisdiction over umbrella clause claims where the party to the contract was a sub-state entity, the conduct of which was attributable to the host state under international law.[35] Other tribunals instead

---

33) *Continental Casualty Company v. The Republic of Argentina,* ICSID Case No. ARB/03/9, Award dated September 5, 2008, 297.

34) *See, e.g., AMTO v. Ukraine,* under the Energy Charter Treaty, 110 ("The so-called umbrella clause of the ECT is of a wider character in that it imposes a duty on the Contracting Parties 'to observe any obligations it has entered into with an Investor or an Investment of the other Contracting Party.' This means that the ECT imposes a duty not only in respect of the investor which is otherwise customary in an investment treaty context, but also vis-à-vis a subsidiary company, established in the host state. This means that an undertaking by Ukraine of a contractual nature vis-à-vis [the investor's local subsidiary] could very well bring into effect the umbrella clause."). However, investors should caution their expectations as to this interpretation prevailing in all instances: for instance, in the *Azurix v. Argentina case, supra,* the tribunal decided against contracts entered into by the claimant's subsidiary being covered by the umbrella clause in the Argentina-United States BIT, despite the use of the wording "with regard to investments" in the umbrella clause.

35) *See Noble Ventures v. Romania,* 68, 79-80; *Eureko v. Poland,* 115-134; *Al-Bahloul v.*

have applied municipal law to determine whether the entity party to the underlying contract had a personality distinct from the host state, in which case the contract was deemed not to fall within the scope of the umbrella clause.[36]

IV. Use of A Most-Favoured-Nation Clause to Enhance Umbrella Clause Protection

A foreign investor may use a most-favoured-nation ("MFN") clause to enhance the protections that the applicable treaty extends, namely by importing protections (such as an umbrella clause) that may otherwise be lacking from another investment treaty concluded by the host state.

To our knowledge, all Korean investment treaties contain an MFN clause. A typical MFN clause reads as follows:

> *"(1) Neither Party shall in its territory subject investments effected by, and income accruing to, investors of the other Party to treatment less favourable than that which it accords to investments effected by, and income accruing to, investors of any third State.*

Tajikistan, 269 ("the joint venture agreements are not obligations undertaken by a State organ, but rather by State-owned enterprises, and there is no basis for concluding that the State-owned enterprises signed these agreements acting in a governmental capacity…"); *Bosh v. Ukraine,* 241 *et seq.* ("As the Tribunal has concluded above that the conduct of the University is not attributable to Ukraine, it follows that it cannot be said that Ukraine, as a 'Party', has entered into any obligations… with regard to investment. Rather, if the umbrella clause is going to have the effect argued for by the Claimants, it could only do so in respect of obligations that have been assumed by the host State or by an entity whose conduct is attributable to the host State"); and *BIVAC v. Paraguay,* 141.

36) *See Impregilo S.p.A. v. Islamic Republic of Pakistan,* ICSID Case No. ARB/03/3, Decision on Jurisdiction dated April 22, 2005, 223. *See also Azurix v. Argentina,* 384, in which tribunal held that a contract entered into by the local subsidiary of the claimant with the province of Buenos Aires was not covered by the umbrella clause; *AMTO v. Ukraine,* 109 *et seq.; EDF v. Romania,* 317 and 319 ("There is in principle no responsibility by the State for such breach in the instant case since the State, not being a party to the contract, has not directly assumed the contractual obligations the breach of which is invoked… Attribution does not change the extent and content of the obligations arising under the [contract], that remain contractual, nor does it make Romania party to such contracts"); and *Gustav F W Hamester GmbH & Co KG v. Republic of Ghana,* ICSID Case No. ARB/07/24, Award dated June 18, 2010, 343 et seq.

> *(2) Neither Party shall in its territory subject investors of the other Party, as regards their management, use, enjoyment or disposal of their investment, as well as to any activity connected with these investments, to treatment less favourable than that which it accords to investors of any third State."*[37]

Foreign investors have used MFN clauses in the "basic treaty" with a host state that protects them and their investment to import into that basic treaty more favourable treatment offered to investors in a "third state treaty" between the same host state and third states.

The use of MFN clauses to import substantive protections from one investment treaty to another has been uncontroversial in the jurisprudence. There are several examples of states being held liable for breach of treatment provisions that did not exist in the basic treaty and were imported from a third state treaty via an MFN clause. As a recent illustration, in *White Industries v. India,* an Australian investor brought a case against India under the Australia-India BIT. The Australia-India BIT contained an MFN clause similar to the one reproduced above. White Industries successfully relied on the MFN clause to import an "effective means" provision from the India-Kuwait BIT, which provided that "Each Contracting State shall, in accordance with its applicable laws and regulations, provide effective means of asserting claims and enforcing rights with respect to investments." The tribunal found that India's conduct breached "effective means" provision imported into the Australia-India BIT and thereby breached the MFN clause in that treaty.[38]

Turning to umbrella clauses more particularly, while a large number of Korean investment treaties contain an umbrella clause, some do not, such as the Korea-United States FTA. An investor bringing a claim under a Korean investment treaty that does not contain an umbrella clause could rely on the MFN clause in that treaty to import an umbrella clause from another investment treaty concluded by the host state. For instance, a Korean investor under the Korea-

37) *See* Article 4 of the Korea-Indonesia BIT.

38) *White Industries Australia Limited v. The Republic of India,* UNCITRAL, Award dated November 30, 2011.

United States FTA could import the umbrella clause from the Argentina-United States BIT. Such use of an MFN clause is precisely what happened in the recent EDFI v. Argentina case. In that case, the tribunal allowed the French investor EDFI to use the MFN clause of the applicable France-Argentina BIT to import an umbrella clause from another Argentine BIT. The tribunal ultimately held that Argentina had breached the imported umbrella clause.

These cases show what a powerful tool an MFN clause can be for foreign investors to enhance their investment treaty protections.

V. Conclusion

There remain a number of uncertainties—which are unlikely to be lifted in the near future—as to the protection that umbrella clauses effectively offer. Still, foreign investors have been able to bring successful claims for breach of umbrella clauses in a number of cases to date, with respect to undertakings given by the host state both in contracts and in legislation.

The two noted changes in Korea's drafting policy with respect to umbrella clauses may indicate a willingness on the part of the Korean Government to minimise or exclude the impact of umbrella clauses: first, the location of umbrella clauses, where present, has been moved from the treatment provision towards the end of the treaties and, second, in recent treaties, Korea has abandoned altogether including umbrella clauses. However, these two changes are unlikely to affect the availability of umbrella clause protection under Korean investment treaties: (i) as regards Korea moving the location of umbrella clauses toward the end of the treaties, with rare exceptions, arbitral tribunals have not considered the location of the umbrella clause to be relevant to its interpretation and effect; and (ii) as regards Korea refraining from including umbrella clauses in its latest investment treaties, the jurisprudence show that if a treaty contains an MFN clause (which Korean investment treaties do), the investor will be able to import an umbrella clause from another investment treaty and thereby will still benefit from umbrella clause protection.

In view of the number of Korean investment treaties that contain an umbrella

clause or an MFN clause, investors covered by these treaties thus should be aware of the additional protection that umbrella clauses may offer.

References

Alexandrov, Stanimir A., "Breaches of Contracts and Breaches of Treaty - The Jurisdiction of Treaty-Based Arbitration Tribunals to Decide Breach of Contract Claims in SGS v. Pakistan and SGS v. Philippines," Journal of World Investment & Trade, Vol.5 No.4, August 2004, pp. 555 *et seq.*

Cohen Smutny, Abby and Lee, Steven, "Chapter 15 The MFN Clause: What Are Its Limits," in Katia Yannaca-Small, *Arbitration Under International Investment Agreements - A Guide to the Key Issues,* Oxford University Press, 2010.

Dolzer, Rudolf and Schreuer, Christoph, *Principles of International Investment Law,* Oxford University Press, 2nd ed., 2012, pp. 166 et seq.

Gaillard, Emmanuel, "A Black Year for ICSID," New York Law Journal, March 1, 2007.

Gaillard, Emmanuel, "Investment Treaty Arbitration and Jurisdiction over Contractual Claims - The SGS v. Pakistan and SGS v. Philippines precedents," in T. Weiler (ed), *International Investment Law and Arbitration - Leading Cases from the ICSID, NAFTA, Bilateral Investment Treaties and Customary International Law,* Cameron May, 2005.

Gaillard, Emmanuel, *La Jurisprudence du CIRDI,* Pedone, 2004, pp. 759 *et seq.* and pp. 833-835.

Gallus, Nick, "An Umbrella Just for Two? BIT Obligations Observance Clauses and the Parties to a Contract," Arbitration International, Vol.24 No.1, 2008, pp. 157 *et seq.*

"Lone Star Claims Against South Korea Has An Arbitral Tribunal in Place," Investment Arbitration Reporter, Retrieved May 13, 2013 from http://www.iareporter.com/articles/20130513

OECD, "The Interpretation of the Umbrella Clause in Investment Agreements," Working Papers on International Investment, No 2006/3, October 2006.

Schreuer, Christoph H., "Travelling the BIT Route - Of Waiting Periods, Umbrella Clauses and Forks in the Road," Journal of World Investment & Trade, vol. 5, no. 2, April 2004, pp.231 *et seq.*

Weiler, T.G. (ed.), "Part I - Umbrella Clause," *Investment Treaty Arbitration and International Law,* JurisNet, 2008.

Azurix v. Argentine Republic, ICSID Case No. ARB/01/12, Award dated July 14, 2006.

Bosh International, Inc. et al. v. Ukraine, ICSID Case No. ARB/08/11, Award dated October 25, 2012.

Bureau Veritas, Inspection, Valuation, Assessment and Control, BIVAC B.V. v. The Republic of Paraguay, ICSID Case No. ARB/07/9, Decision of the Tribunal on Objections to Jurisdiction dated May 29, 2009.

Burlington Resources Inc. v. Republic of Ecuador, ICSID Case No. ARB/08/5, Decision on Jurisdiction dated June 2, 2010.

Burlington Resources Inc. v. Republic of Ecuador, ICSID Case No. ARB/08/5, Decision on Liability dated December 14, 2012.

CMS Gas Transmission Company v. The Republic of Argentina, ICSID Case No. ARB/01/8, Award dated May 12, 2005.

CMS Gas Transmission Company v. The Republic of Argentina, ICSID Case No. ARB/01/8, Decision of the *Ad Hoc* Committee on the Application for Annulment dated September 25, 2007.

Compañiá de Aguas del Aconquija S.A. and Universal v. Argentine Republic, ICSID Case No. ARB/97/3, Decision on Annulment dated July 3, 2002.

Consortium Groupement L.E.S.I.- DIPENTA v. République algérienne démocratique et populaire, ICSID Case No. ARB/03/08, Award dated January 10, 2005.

Continental Casualty Company v. The Republic of Argentina, ICSID Case No. ARB/03/9, Award dated September 5, 2008.

Duke Energy Electroquil Partners & Electroquil S.A. v. Republic of Ecuador, ICSID Case No. ARB/04/19, Award dated August 18, 2008.

EDF International S.A., SAUR International S.A. and León Participaciones Argentinas S.A. v. Argentine Republic, ICSID Case No. ARB/03/23, Award dated June 11, 2012.

El Paso Energy International Company v. The Argentine Republic, ICSID Case No. ARB/03/15, Decision on Jurisdiction dated April 27, 2006.

Enron Corporation and Ponderosa Assets, L.P. v. Argentine Republic, ICSID Case No. ARB/01/3, Award dated May 22, 2007.

Eureko BV v. Republic of Poland, Partial Award dated August 19, 2005.

Gustav F W Hamester GmbH & Co KG v. Republic of Ghana, ICSID Case No. ARB/07/24, Award dated June 18, 2010.

Impregilo S.p.A. v. Islamic Republic of Pakistan, ICSID Case No. ARB/03/3, Decision on Jurisdiction dated April 22, 2005.

Joy Mining Machinery Limited v. The Arab Republic of Egypt, ICSID Case No. ARB/03/11, Award on Jurisdiction dated August 6, 2004.

LG&E Energy Corp. et al. v. Argentine Republic, ICSID ARB/02/1, Award dated July 25, 2007.

Liman Caspian Oil BV and NCL Dutch Investment BV v. Republic of Kazkhstan, ICSID Case No. ARB/07/14, Award dated June 22, 2010.

Limited Liability Company Amto v. Ukraine, SCC Case No. 080/2005, Final Award dated March 26, 2008.

Mohammad Ammar- Al-Bahloul v. Tajikistan, SCC Case No. V(064/2008), Partial Award on Jurisdiction and Liability dated June 18, 2010.

Noble Ventures, Inc v. Romania, ICSID Case No. ARB/01/11, Award dated October 12, 2005.

Pan American Energy LLC and BP Argentina Exploration Company v. Argentine Republic, ICSID Case No. ARB/03/13 and *BP America Production Co. and Others v. Argentine Republic,* ICSID Case No. ARB/04/8, Decision on Preliminary Objections dated July 27, 2006.

S*empra Energy International v. The Argentine Republic,* ICSID Case No. ARB/02/16, Award dated September 28, 2007.

SGS Société Générale de Surveillance S.A. v. The Republic of Paraguay, ICSID Case No. ARB/07/29, Decision on Jurisdiction dated February 12, 2010.

S*GS Société Générale de Surveillance S.A. v. The Republic of Paraguay,* ICSID Case No. ARB/07/29, Award dated February 10, 2012.

SGS Société Générale de Surveillance S.A. v. Republic of the Philippines, ICSID Case No. ARB/02/6, Decision of the Tribunal on Objections to Jurisdiction dated January 29, 2004.

Siemens A.G. v. Argentina, ICSID Case No. ARB/02/08, Award dated February 6, 2007.

White Industries Australia Limited v. The Republic of India, UNCITRAL, Award dated November 30, 2011.

Website
http://www.unctadxi.org/templates/DocSearch____779.aspx
http://www.mofat.go.kr
http://aric.adb.org/FTAbyCountryAll.php