



Application Of The Umbrella Article Rule In Bilateral Investment Agreements International Practice

Rajabov Adkham Amrulloevich,

Lecturer Of “Business Law” Department Of Tashkent State Law University, Uzbekistan

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ABSTRACT

The Bilateral Investment Treaty (BIT) is the most common type of agreement in private international law to protect the rights and legitimate interests of investors. According to UNCTAD, more than 2,500 bilateral investment agreements have been signed between the two countries to date. The study found that 40 percent of them applied the “Umbrella clause” rule. The article examines the scientific and theoretical views of international economists and jurists, the analysis of existing contracts under the Umbrella clause, as well as international practice in this area, and defines the Umbrella clause rule. The analysis revealed the pros and cons of the "Umbrella Clause" rule, the advantages and disadvantages of law enforcement practice under this rule. The impact of the "Umbrella clause" rule on the outcome of bilateral investment disputes has been evaluated. At the same time, the lack of a uniform approach to the application of contract terms under the "Umbrella clause" rule in international arbitration has been described as a constant source of disagreement. The article discusses the prospects for the application of the “Umbrella clause” rule in bilateral investment agreements.

KEYWORDS

Umbrella Clause, Bilateral Investment Agreement, International Legal Guarantees, Foreign Investor, Host Country, Model Agreement, Obligation.

INTRODUCTION

One type of agreement in private international law that protects the rights of investors and safeguards their legitimate interests is the bilateral investment treaty (BIT). According to UNCTAD, the two countries have signed more than 2,500 bilateral investment agreements. [1]. The first bilateral investment agreement was signed in 1959 between the Federal Republic of Germany and Pakistan. These agreements are also divided into types of agreements that contain different content. While some of these relate only to disputes arising from a default under the same agreement or breach of other requirements of the agreement, others provide for any investment-related disputes. However, some agreements impose obligations on the host country. For example, these obligations may include "compliance with any obligations," "guarantee of obligations and continued compliance with those guarantees," "performance of any obligations assumed," and other investment requirements [p.2, 8]. The obligations in this context are conditions under the "Umbrella Clause".

Forty percent of bilateral investment agreements are governed by the "Umbrella clause". Any bilateral investment agreement entered into by countries such as Switzerland, Germany, the United Kingdom and the Netherlands shall include this provision. It is used in some cases in agreements concluded by France, Australia and Japan.

The "Umbrella clause" is one of the international legal guarantees for foreign investors provided for in bilateral investment agreements. The "Umbrella clause" is a guarantee mechanism, as the name implies.

This agreement represents a state guarantee for all investment commitments made in bilateral agreements [3].

The "Umbrella clause" has been variously defined by economists and lawyers as an international legal guarantee.

For example, according to V.M Shumilov, a guarantee under the Umbrella clause is a measure aimed at insuring investments against risks arising from political events and actions of the state government in which the investment is made. [p.4, 260]

Or, according to A. Ya Sukharev and V. E. Krutskikh, an international guarantee is a guarantee given by any state or group of states to other participants in international relations to fulfill obligations or maintain a certain level of international relations, as well as to ensure compliance with established rights and guarantees. [p.5, 111]

In the UNCTAD rules, the "Umbrella clause" stipulates that all obligations under the investment agreement between the investor and the state must be observed. In this case, the terms of the investment agreement should be supplemented by the application of the rule "Umbrella clause" in case of violation of the terms of the agreement.[6] In addition, D.M. Yulov in his literature states that the rule "Umbrella clause" is one of the international legal guarantees of the rights of foreign investors who have concluded a bilateral investment agreement, according to which the receiving state of foreign capital provides a package of guarantees. [p.7, 202] According to V.Zivkovich, the Umbrella clause is a mechanism that turns pure contractual

disputes into disputes under international agreements. This mechanism ensures that the dispute over the contract is considered in international arbitration.[8]

Shroyer said the Umbrella clause is an additional guarantee for the investor and defines its protection based on traditional international standards. If the investor's right under the investment agreement has been violated, then it is also a violation of the bilateral investment agreement. [p.9, 141]A.S. Yukhno The rule of the Umbrella clause is that the parties have the right to apply to international arbitration for an impartial and correct settlement of a dispute over foreign investment. [10]

The Umbrella clause rule was first enshrined in a 1921 intergovernmental agreement between Great Britain and Peru. According to him, disputes arising from the concession provided by the Peruvian government to the British company will be resolved by the ad hoc tribunal. Thus, for the first time, the Peruvian state has an international legal obligation to the UK under a concession agreement with the company.

By the 1950s, the“Umbrella clause” was enshrined in bilateral investment model agreements between West Germany and the United Kingdom.

According to Article 2(paragraph 2) of the U.K. Model Agreement on the Attraction and Reciprocal Protection of Investments, "The parties to the agreement must comply with any obligations arising from investments by nationals or companies of the other party .[11]

According to Article 7, paragraph 2, of the German Model Agreement on the Promotion

and Reciprocal Protection of Investments, "Each Contracting State shall fully fulfill its obligations to investors of other Contracting States in its territory.".[12]

The Model Agreement on the Promotion and Reciprocal Protection of Investments of the Russian Federation does not provide for the Umbrella clause, but it is reflected in some bilateral agreements between Russia and other countries.[p.13, 56]This is directly related to the view in Russia that the Umbrella clause rule could harm state sovereignty.

According to the experience of Germany and the United Kingdom, any bilateral investment agreement concluded by these countries should include the Umbrella clause. In Russian experience, however, no such obligation has been established.

The Umbrella clause rule was first applied in a dispute between the company and the Iranian government over the nationalization of the Anglo-Iranian oil company.[p.14, 6]This means that the UK has considerable experience in applying this rule.

Resolution of the Cabinet of Ministers of the Republic of Uzbekistan No. 180 of August 2, 2005 approved the Regulation "On the procedure for concluding, amending, terminating and implementing investment agreements between the Government of the Republic of Uzbekistan and a foreign investor". As an appendix to the Regulation, there is a model investment agreement between the Government of the Republic of Uzbekistan and a foreign investor for the implementation of an investment project. However, neither the Charter nor the model contract provides for the Umbrella clause [15]. At the same time,

conditions are included for the settlement of disputes and disputes in international arbitration.

Under the 1965 Washington Convention on the International Center for the Settlement of Investment Disputes, bilateral (interstate or intergovernmental) agreements or contracts with an investor in an international center must be enforced by the State party. Such decisions shall not be subject to the procedure for recognition and enforcement of decisions of foreign courts by domestic courts or the Ministries of Justice. Thus, investment agreements and the Washington Convention serve as an international legal protection shield for foreign investors.

Although the “Umbrella clause” applies to 40 per cent of all bilateral investment agreements, as noted above, international law enforcement practice varies. That is, the rule of the Umbrella clause is interpreted and applied differently in each arbitration case or when the parties are settling a dispute. According to Prof. G.M Velyaminov, the “Umbrella clause” is similar to the “Troia horse” and serves to violate the concept of dualism in international law, as well as used in different interpretations in the international transformation of the national obligation of the state.[p.17, 337]

There is no single case law in international investment arbitration on the interpretation and application of the Umbrella clause in resolving investment disputes.[p.18, 8]

Many cases can be cited as examples. “SGS v. Pakistan's investment dispute is one of them. The dispute is part of the Pakistani government's Société Générale de Surveillance S.A. (“SGS”) began with the filing of an

arbitration claim under national law to terminate an investment agreement with a foreign investor. The investor, in turn, has filed a lawsuit against the Pakistan government at the International Center for the Settlement of Investment Disputes. The basis for applying to the international center was a bilateral investment agreement between Pakistan and Switzerland. As noted above, in accordance with the Swiss Model Agreement on Bilateral Investment, such agreements shall be amended to read as follows the Umbrella clause: “Each Contracting Party shall consistently guarantee the observance of the obligations of the other Contracting Party to its investors' investments.” The same condition was contained in the investment agreement between Pakistan and Switzerland.[19]

The International Centre for Settlement of Investment Disputes rejected the investor's claim. In principle, the Center stated that the “Umbrella clause” does not determine independently whether an investment dispute is subject to international investment arbitration, but can only hear the case with the written consent of both parties to the Agreement. It was also found that the literal interpretation of bilateral investment agreements did not provide a clear expression of the “Umbrella clause” rule.[20]

The International Center for Investment Dispute Resolution has narrowly interpreted the “Umbrella clause” in this case. In the same way, “Joy Mining Machinery Limited v. Arab Republic of Egypt”[21], “CMS Gas Transmission Company v. Argentine Republic ”[22] and El Paso Energy International Company v. Argentine Republic ”[23] cases.

“Eureko B.V. v. In the Republic of Poland, [24] the International Center took a different approach. Here, too, special attention is paid to the verbal interpretation of the terms of the bilateral investment agreement. There has also been a broad interpretation of the “Umbrella clause” rule. “Eureko B.V. v. In the case of the Republic of Poland, the Center found the “must be observed” rule in the “Umbrella clause” of the contract to be an imperative norm. It was concluded that “any obligation” means all the obligations of the state in relation to investment, and it was agreed to consider the proceedings of the business center.

Almost simultaneously with this study, the “Salini Costruttori S.p.A. and Italstrade S.p.A. v. In the Hashemite Kingdom of Jordan, [25] the Center stated that it was not authorized to review the dispute. The zoning clause in Article 2, paragraph 4 of the bilateral investment agreement between Italy and Jordan provides that “each Contracting Party shall establish and provide to investors a legal basis to ensure that the political regime in its territory shall not be altered”[26]. The Center did not recognize this provision as “Umbrella clause” in Article 2.4 of the Agreement. According to the arbitrators, the norm provided that states create a legal basis for investment guarantees, but did not impose on them the obligation to comply with the obligations under the investment agreement.

Another aspect of the issue is that a foreign investor can sue the Government in international arbitration only if the investment agreement with the Government stipulates that the parties may apply for arbitration. In this case, the procedure for applying to arbitration specified in the contract must be followed. This procedure may include the

possibility of recourse to international arbitration “if the parties do not reach a mutual agreement on the dispute within six months”, “if they are dissatisfied with the arbitral award provided for in the contract”.

Based on the above, the following conclusions can be drawn about the application of the “Umbrella clause” rule in bilateral investment agreements:

- 1) The “Umbrella clause” rule applies only if one party to the investment agreement is an investor and the other is a direct state. No other legal entity may assume its obligations in lieu of the State;
- 2) The “Umbrella clause” applies only to the performance of contractual obligations under a bilateral investment agreement and does not affect the scope of contractual rights and obligations;
- 3) The “Umbrella clause” may be applied to certain obligations assumed by the State;
- 4) The “Umbrella clause” requires the state to fulfill all obligations under investments, including obligations under bilateral investment agreements. These may include capital investment protection, capital investment regime, transfer of payments, subrogation, restriction of expropriation, and compensation for losses. In addition, the Umbrella clause covers the obligations of the state under other international bilateral and multilateral investment agreements, as well as national civil and administrative legislation;

- 5) The main purpose of the Umbrella clause is to give the parties the right to exercise their rights, the other party to apply to impartial investment arbitration to ensure the fulfillment of its obligations. The decision of the arbitral tribunal is binding on both parties - the state or the investor (individual or legal entity);
- 6) “Umbrella clause” allows the interested party to raise the dispute over a separate (individual) investment agreement with the state to the level of an investment agreement and bring the dispute to investment arbitration, but this rule is accepted differently by experts, in some cases creates a reverse practice;
- 7) The concept of international dualism emerged in international law because the "Umbrella clause" was formed at the junction of public international law and private international law. According to him, the investor must protect his rights under the investment agreement through the diplomatic protection of his country. The investor's country is treated as a third party in investment disputes;
- 8) The “Umbrella clause” serves to create an acceptable investment climate, but there is a risk that one of the parties may be abused due to a conscientious approach to this rule;
- 9) The lack of a unified approach to understanding the “Umbrella clause” requires the development of a unified approach that combines the efforts of the expert community on public and international investment. The creation of a single approach will be equally

beneficial for both investors and the state..

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