Where Both Worlds Meet: Contractual Waiver of Liability and the Contract-Treaty Divide

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The problem of the law applicable to State contracts (i.e. contracts concluded between a foreign national and a State or a state entity) as well as the responsibility of States for the breach of these contracts has entertained the minds of scholars and practitioners ever since the famous PCIJ *dictum* in the 1929 *Serbian Loans* case:

> "Any contract which is not a contract between States in their capacity as subjects of international law is based on the municipal law of some country. The question as to which this law is forms the subject of that branch of law which is at the present day usually described as private international law or the 'doctrine of the conflict of laws'." (*Case concerning the Payment of Various Serbian Loans Issued in France*, Permanent Court of International Justice Judgment Series A No. 20 (1929) at p. 41)

It is a long-established principle of international law that "the breach by a State of a contract does not as such entail a breach of international law." (see the *ILC Draft Articles on Responsibility of States for Internationally Wrongful Acts*, Commentary 6 to Article 4)

The *Vivendi* Annulment Committee prominently held in relation to the contract-treaty dichotomy that:

> "95. As to the relation between breach of contract and breach of treaty… it must be stressed that… [a] State may breach a treaty without breaching a contract, and vice versa …
> 96. In accordance with this general principle (which is undoubtedly declaratory of general international law), whether there has been a breach of the BIT and whether there has been a breach of contract are different questions. Each of these claims will be determined by reference to its own proper or applicable law – in the case of the BIT, by international law; in the case of the Concession Contract, by the proper law of the contract, in other words, the law of Tucumán." (*Vivendi v. Argentina*, ICSID Case No. ARB/97/3, Decision on annulment of July 3, 2002, paras 95-96)

There is a consistent line of case law in the practice of ICSID tribunals upholding the submission that "not any breach of an investment contract could be regarded as a breach of a BIT." (*Salini v. Jordan*,

ICSID Case No. ARB/02/13, Decision on Jurisdiction of November 15, 2004, para. 154; see also *Impregilo v. Pakistan*, ICSID Case No. ARB/03/3, Decision on Jurisdiction of April 22, 2005, para. 260; *El Paso v. Argentina*, ICSID Case No. ARB/03/15, Decision on Jurisdiction of April 27, 2006, para. 77; *Noble Ventures v. Romania*, ICSID Case No. ARB/01/11, Award of October 12, 2005, para. 53)

There are two explanations for this proposition:

a. **first**, historically, host States would not accept the interference by means of diplomatic protection or otherwise of the State of nationality for the mere breach of a contract concluded with the foreign national concerned;

b. **secondly**, this may be due to the old, but surviving idea that municipal and international law are two systems existing in parallel, which do not directly interact. (see Fitzmaurice, G., *The General Principles of International Law*, 92 Recueil des Cours (1957-II) at pp. 68-94) There are examples found in the ICSID case law which continue to speak of international law and municipal law as two "differing legal orders." In the landmark *SGS v. Pakistan* arbitration the tribunal recognized that

> "[a]s a matter of general principle, **the same set of facts** can give rise to different claims grounded on differing legal orders: the municipal and the international legal orders." (*SGS v. Pakistan*, Decision on objections to Jurisdiction of August 6, 2003, para.147, emphasis added; see also, *Pan American & BP Argentina v. Argentina*, ICSID Case No. ARB/03/13, Decision on preliminary objections of July 27, 2006, para. 110).

ICSID tribunals retain a claim based on a breach of contract in two instances:

a. **where** there is an umbrella clause contained in the applicable BIT;

b. **where** the contract breach may otherwise be assimilated as a breach of other substantive standards of protection found in a BIT, i.e. where the State acted as a sovereign (holder of the "*puissance publique*") and not as an ordinary contracting party and its actions involved "an obviously arbitrary or tortious element." (*El Paso v. Argentina*, Decision on Jurisdiction of April 27, 2006, para. 77)

A relatively recent ICSID award in the case of *Toto v. Lebanon* (*Toto v. Lebanon*, ICSID Case No. ARB/07/12, Award of June 7, 2012) adds new insights to this contract-treaty dichotomy. This award has passed somewhat unnoticed, but contains important findings of law.

The tribunal in *Toto v. Lebanon* dealt with the implications of contractual waiver of liability in the context of investment treaty arbitration. While the contract and the treaty belong to two "differing legal orders", it turned out that they meet at the point of the waiver.

The dispute arose from a 1997 Contract entered into between Toto Costruzioni Generali S.p.A. ("Toto"), a company incorporated under the laws of Italy, and Lebanon, acting through *Conseil Executif des Grands Projets* ("CEGP"), for the construction of a portion of the Arab Highway. Toto claimed the amount of over US$ 41 million (including moral damages) in compensation for various delays on the part of Lebanon, such as failure to carry out the necessary site expropriations, failure to deliver sites and failure to remove Syrian troops from the sites which have led to a 4-year extension of the contractually provided time for completion of the project. During that extra time, however, Toto obtained several extensions of time in exchange of Toto's waiver of liability. These waivers were contained in Addendum No. 2 to the Contract. (see paras 65-67; 77; 81; 83 of the Award)

In view of the above mentioned contract-treaty divide, Toto tried to persuade the tribunal that the waivers it had signed are only contractual in character and do not extend to its treaty claims. In effect, Toto argued that it is entitled to compensation for the treaty breaches notwithstanding the waivers of liability under municipal law. (para. 83 of the Award)

The tribunal did not accept this line of argument and determined that:

> "85. [A]s stated repeatedly, the Tribunal is concerned by claims of Treaty breaches, and not by breaches of the Contract. Toto's waiver of its right to invoke the CEGP's liability under the Contract to claim contractual damages does not affect its right to invoke Lebanon's breach of the Treaty before this Tribunal. However… the assessment of damages and of the compensation to be granted for a Treaty breach may be affected by a waiver not to claim compensation under the Contract, when both damage claims cover the same harm. Indeed, **when it concerns the same damage for the same act, compensation that a Claimant has waived under the Contract cannot be recovered under the Treaty**." (emphasis added)

This conclusion shows that investors should be vigilant in signing contractual waivers in the delusion that they will not affect their treaty claims. Although the contractual waiver belongs to a different legal order, an investor cannot "approbate and reprobate in respect of the same contract." (*SGS v. Philippines*, ICSID Case No. ARB/02/6, Decision on objections to Jurisdiction of January 29, 2004, para. 155) In other words, the Claimants will not be let to "have the best of both worlds" in like cases.

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