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International Arbitration Case Law

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SGS SOCIÉTÉ GÉNÉRALE DE SURVEILLANCE S.A. v. REPUBLIC OF THE PHILIPPINES (ICSID CASE NO. ARB/02/6) AWARD ON JURISDICTION

Case Report by Charles B. Rosenberg**
Edited by Ignacio Torterola***

An Award on Jurisdiction rendered on January 29, 2004, under the Switzerland-Philippines bilateral investment treaty, and in accordance with the ICSID Convention and Arbitration Rules.

Tribunal:	Dr. Ahmed S. El-Kosheri (President), Professor James Crawford, Professor Antonio Crivellaro
Claimant's counsel:	Mr. Jean-Pierre Méan and Mr. Andrea Rusca, SGS SOCIÉTÉ GÉNÉRALE DE SURVEILLANCE S.A.; and Mr. Emmanuel Gaillard and Mr. John Savage, SHEARMAN & STERLING.
Defendant's Counsel:	Ms. Judith Gill and Mr. Matthew Gearing, ALLEN & OVERY; Professor Christopher Greenwood, QC; Undersecretary Mr. Manuel A. J. Teehankee; DEPARTMENT OF JUSTICE, PHILIPPINES; and Assistant Secretary Mr. Emmanuel P. Bonoan, DEPARTMENT OF FINANCE, PHILIPPINES.

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INDEX OF MATTERS DISCUSSED

1. Facts of the Case 1
2. Legal Issues Discussed in the Decision 2
   (a) Precedent in international law (paras. 95-97) 2
   (b) Was there an investment "in the territory of" the Philippines? (paras. 99-112) 3
   (c) Jurisdiction under the umbrella clause (paras. 113-129) 4
   (d) Jurisdiction over contractual claims (paras. 130-135) 5
   (e) The exclusive choice of forum clause (paras. 136-155) 6
   (f) Is there a BIT claim independent of the CISS Agreement? (paras. 156-164) 8
   (g) The retrospectivity issue (paras. 165-168) 9
3. Decision 10

Digest

1. Facts of the Case

On August 23, 1991, SGS Société Générale de Surveillance S.A. ("SGS"), a Swiss corporation, concluded a three-year agreement with the Philippines (the "CISS Agreement"), under which SGS would provide specialized services to assist in improving the customs clearance and control processes of the Philippines. Under the CISS Agreement, SGS agreed to carry out, on an exclusive basis, pre-shipment inspection in any country of export to the Philippines. SGS also agreed to provide the Philippines with certain assistance, including: (i) training various Philippines agencies, in particular the Philippines Bureau of Customs ("BOC"); (ii) providing customs equipment and maintaining that equipment; and (iii) supplying customs consultants to carry out feasibility studies and evaluate the BOC's computer needs. SGS further agreed to maintain a liaison office in the Philippines. The Philippines agreed to pay SGS a fee amounting to 0.6% of the FOB value declared on the exporter's final settlement invoice covering each shipment inspected. Article 12 of the CISS Agreement required that contractual disputes be submitted to specified courts in the Philippines to be decided in accordance with Philippines law. The CISS Agreement was subsequently amended and extended by the parties until March 31, 2000, at which time SGS's services under the CISS Agreement were discontinued primarily due to implementation of the GATT-WTO Valuation System which reduced the need for physical inspection of imports.[1]

During the period of performance of the CISS Agreement, SGS invoiced the BOC approximately $680 million for inspections performed in a large number of countries. Of the amount involved for these inspections, some $540 million was actually paid. SGS thus claimed CHF 202,413,047.36 (approximately $140 million) unpaid under the amended CISS Agreement. In March 2001, the Secretary of Finance of the Philippines directed the BOC to establish a joint review team with SGS to determine the total amount due. The BOC-SGS Review Team reported on October 25, 2001 that of the amount claimed by SGS: (i) CHF 192,420,782.26 was payable to SGS; (ii) CHF 3,737,190.78 should be withheld in favor of the Philippines; and (iii) the balance of CHF 9,992,265.10 was unresolved. After SGS indicated that it was prepared to forego payment of the unresolved balance (CHF 9,992,265.10) if agreement could be reached on financing the amount determined by the Review Team to be payable to SGS

[1] Award ¶ 14.

(CHF 192,420,782.26), the Secretary of Finance wrote to the financial adviser of SGS stating: "[w]e have no reason to reject the findings of the said report and, accordingly, efforts may now be directed to finding ways and means to settle the amount unanimously determined to be payable to SGS, subject to applicable laws and regulations."[2]

In January 2002, the Philippines made "a token good faith payment" of PHP 1 million (approximately $20,000) to SGS. No further payments were made or agreements reached. As a consequence, SGS commenced ICSID arbitration proceedings on April 26, 2002 pursuant to the Swiss Confederation-Republic of the Philippines Agreement on the Promotion and Reciprocal Protection of Investments (the "BIT"). SGS claimed that by failing to pay the CHF 202,413,047.36 claimed by SGS, the Philippines was in breach of Articles IV(1) (unreasonable or discriminatory measures), IV(2) (fair and equitable treatment), VI(1) (expropriation), and X(2) of the BIT (umbrella clause).

2. *Legal Issues Discussed in the Decision*

(a) Precedent in international law (paras. 95-97)

The Tribunal noted that the main issues in this case were discussed at some length by the ICSID tribunal in *SGS v. Pakistan*. That case involved an investment agreement between SGS and Pakistan that provided for analogous services to those in the present case. The Tribunal, however, made clear that it did not agree with all of the conclusions reached by the *SGS v. Pakistan* tribunal regarding the interpretation of similar language in the Switzerland-Philippines BIT.

According to the Tribunal, it was not bound to defer to the conclusions reached by the *SGS v. Pakistan* tribunal for the following reasons. First, the Tribunal interpreted Article 53(1) of the ICSID Convention – which provides that ICSID awards are "binding on the parties" – as directed to the *res judicata* effect of awards, rather than their impact as precedents in later cases. Second, the Tribunal explained that "although different tribunals constituted under the ICSID system should in general seek to act consistently with each other, in the end it must be for each tribunal to exercise its competence in accordance with the applicable law, which will by definition be different for each BIT and each

[2] Award ¶ 37.

Respondent State."[3] Third, the Tribunal noted that "there is no doctrine of precedent in international law" because "[t]here is no hierarchy of international tribunals, and even if there were, there is no good reason for allowing the first tribunal in time to resolve issues for all later tribunals."[4]

(b) Was there an investment "in the territory of" the Philippines? (paras. 99-112)

The Tribunal ruled that SGS made an investment "in the territory of" the Philippines in accordance with Article II of the BIT, which provides that the BIT applies to "investments in the territory of the one Contracting Party . . . by investors of the other Contracting Party."[5] The Tribunal emphasized that investments made outside the territory of the Respondent State, however beneficial to it, would not be covered by the BIT.

The Tribunal found that under the CISS Agreement, SGS was to provide services, within and outside the Philippines, with a view to improving and integrating the import services and associated customs revenue gathering of the Philippines. The focal point of SGS's services under the CISS Agreement was the provision, in the Philippines, of a reliable inspection certificate on the basis of which import clearance could be expedited and the appropriate duty charged. SGS's inspections abroad were carried out to enable SGS to provide, in the Philippines, an inspection certificate on which the BOC could use to enter goods into the customs territory of the Philippines and to assess and collect the ensuing revenue. Those operations were organized through SGS's Manila liaison office, which employed a significant number of people. Indeed, its monthly payroll in the Philippines ranged between $100,000 and $200,000, accounting for a quarter of its total expenses. Accordingly, the Tribunal concluded that these elements taken together are sufficient to qualify the service as one provided in the Philippines.

The Tribunal further reasoned that the fact that the bulk of the cost of providing SGS's service was incurred outside the Philippines was not decisive. Nor was it decisive that SGS was paid in Switzerland. Moreover, the fact that SGS's services were treated as performed abroad for tax purposes was not outcome-determinative: "The tax treatment of investments is a matter for local law with its own regime of rules as to where income is considered to have been earned, a

[3] Award ¶ 97.
[4] *Id.*
[5] Award ¶ 99.

regime distinct from that of the BIT."[6] The Tribunal remarked, however, that its conclusion regarding Article II of the BIT might have been different if SGS had provided the certificates and issued its reports abroad (*e.g.*, to a Philippines trade mission in each country of export), rather than through its Manila liaison office.

The Tribunal agreed with the reasoning of the tribunal in *SGS v. Pakistan*, which had held that equivalent pre-inspection services were provided "in the territory of the host State" because there had been an "injection of funds into the territory of Pakistan for the carrying out of SGS's engagements under the PSI Agreement."[7] Moreover, the Tribunal remarked that the present case seemed stronger for a finding that SGS's investment was made "in the territory of" the Philippines, given the scale and duration of SGS's activity and the significance of the activities of its Manila liaison office.

(c) Jurisdiction under the umbrella clause (paras. 113-129)

The Tribunal concluded that under the umbrella clause in Article X(2) of the BIT – which provides that "[e]ach Contracting Party shall observe any obligation it has assumed with regard to specific investments in its territory by investors of the other Contracting Party" – the Philippines was required to observe the obligation to pay sums properly due and owing under the CISS Agreement.[8] However, this obligation is dependent on the amounts owing being definitively acknowledged or determined in accordance with the CISS Agreement.

The Tribunal interpreted the umbrella clause as "provid[ing] assurances to foreign investors with regard to the performance of obligations assumed by the host State under its own law with regard to specific investments."[9] In other words, Article X(2) makes it a breach of the BIT for the host State to fail to observe binding commitments, including contractual commitments, which it has assumed with regard to specific investments. But this does not mean that the determination of how much money the Philippines is obliged to pay becomes a treaty matter. The extent of that obligation is still governed by the contract, and it can only be determined by reference to the terms of the contract.

In so ruling, the Tribunal diverged from the holding of the tribunal in *SGS v.*

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[6] Award ¶ 107.
[7] Award ¶ 111.
[8] Award ¶ 115.
[9] Award ¶ 126.

Pakistan, which had adopted a highly restrictive interpretation of the umbrella clause that contractual claims could only be brought under the umbrella clause "under exceptional circumstances." The Tribunal disagreed with the *SGS v. Pakistan* tribunal that a broad interpretation of the umbrella clause would involve a full-scale internationalization of domestic contracts that would, in effect, convert investment contracts into treaties. The Tribunal clarified:

> "[T]his is not what Article X(2) of the Swiss-Philippines Treaty says. It does not convert non-binding domestic blandishments into binding international obligations. It does not convert questions of contract law into questions of treaty law. In particular it does not change the proper law of the CISS Agreement from the law of the Philippines to international law. Article X(2) addresses not the *scope* of the commitments entered into with regard to specific investments but the *performance* of these obligations, once they are ascertained."[10]

(d) Jurisdiction over contractual claims (paras. 130-135)

The Tribunal concluded that under Article VIII(2) of the BIT – which provides that an investor may submit an investment dispute "either to the national jurisdiction of the Contracting Party in whose territory the investment has been made or to international arbitration" – the Tribunal has jurisdiction with respect to a claim arising under the CISS Agreement, even though it may not involve any breach of the substantive standards of the BIT.[11]

The Tribunal noted that the plain language of Article VIII of the BIT is *prima facie* an entirely general provision, allowing for submission of all investment disputes by an investor against the host State, regardless of whether the investor's claims are BIT or purely contract claims. The Tribunal's *prima facie* conclusion was supported by the following considerations. First, each of the forums contemplated by Article VIII(2) of the BIT – *i.e.*, the national courts of the host State, ICSID panels, and *ad hoc* tribunals established under the UNCITRAL Rules – has the competence to apply the law of the host State, including its law of contract. Second, if the State Parties to the BIT had wanted to limit investor-State arbitration to claims concerning breaches of the substantive standards contained in the BIT, they would have said so expressly, using the language similar to that

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[10] *Id.*

[11] Award ¶ 130.

used in Article IX of the BIT, *i.e.*, "[d]isputes . . . regarding the interpretation or application of the provisions of this Agreement."[12] Third, allowing investors a choice of forum for resolution of investment disputes of whatever character is consistent with the purpose of the BIT: to promote and protect foreign investments.

The tribunal in *SGS v. Pakistan* had taken the opposite view holding that it had no jurisdiction with respect to SGS's claims based on alleged breaches of a contract which do not also constitute or amount to breaches of the substantive standards of the BIT. While the present Tribunal agreed with the *SGS v. Pakistan* tribunal's concern that the general provisions of BITs should not, unless clearly expressed to do so, override specific and exclusive dispute settlement arrangements made in the investment contract itself, the Tribunal distinguished between "the interpretation of the general phrase 'disputes with respect to investments' in BITs, and the impact on the jurisdiction of BIT tribunals over contract claims (or, more precisely, the admissibility of those claims) when there is an exclusive jurisdiction clause in the contract."

In sum, the Tribunal concluded that: "It is not plausible to suggest that general language in BITs dealing with all investment disputes should be limited because in some investment contracts the parties stipulate exclusively for different dispute settlement arrangements . . . [I]t is possible for BIT tribunals to give effect to the parties' contracts while respecting the general language of BIT dispute resolution provisions."[13]

(e) The exclusive choice of forum clause (paras. 136-155)

The Tribunal concluded that a claim arising under the CISS Agreement that does not involve any breach of the substantive standards of the BIT, brought in breach of the exclusive jurisdiction clause in Article 12 of the CISS Agreement, is inadmissible since Article 12 is not waived or over-ridden by Article VIII(2) of the BIT or by Article 26 of the ICSID Convention. In other words, the Tribunal should not exercise its jurisdiction over a contractual claim when the parties have already agreed on how such a claim is to be resolved, and have done so exclusively. As the Philippine courts are available to hear SGS's contract claim, the Tribunal ruled that "[u]ntil the question of the scope or extent of the

[12] Award ¶ 132(b).
[13] Award ¶ 134.

Respondent's obligation to pay is clarified—whether by agreement between the parties or by proceedings in the Philippine courts as provided for in Article 12 of the CISS Agreement—a decision by this Tribunal on SGS's claim to payment would be premature."[14]

The Tribunal noted that Article 12 of the CISS Agreement is *prima facie* a binding obligation, incumbent on both parties, to resort exclusively to the Philippine courts to resolve any dispute "in connection with the obligations of either party to this Agreement."[15] The Tribunal emphasized that "[t]he basic principle in each case is that a binding exclusive jurisdiction clause in a contract should be respected, unless overridden by another valid provision."[16]

The Tribunal found that neither Article VIII(2) of the BIT nor Article 26 of the ICSID Convention was intended to override an exclusive jurisdiction clause in an investment contract for the following reasons. First, the maxim *generalia specialibus non derogant* instructs that Article VIII of the BIT, which is a general provision applicable to investment arrangements, should not have the effect of overriding specific provisions of particular contracts, freely negotiated between the parties. Second, the maxim *lex posterior derogate legi priori* is inapplicable because that principle only applies as between instruments of the same legal character. By contrast, this case involves a bilateral treaty, which provides the public international law framework for investments between the two States, and a specific contract governed by national law. Third, the *travaux préparatories* of Article 26 of the ICSID Convention makes clear that Article 26 was intended as a rule of interpretation, and not as a mandatory rule. Fourth, the view that Article 26 of the ICSID Convention provides a mandatory override of previously agreed dispute settlement clauses would mean that a party to a contract containing an exclusive jurisdiction clause would obtain an override if it opted for ICSID arbitration, but not if it opted for UNCITRAL arbitration. This consequence could not have been intended.

In the Tribunal's view, this issue concerned the admissibility of the claim and not the jurisdiction of the Tribunal, which is determined by the combination of the BIT and the ICSID Convention. According to the Tribunal, a party should not be allowed to rely on a contract as the basis of its claim when the contract itself

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[14] Award ¶ 155.
[15] Award ¶ 137.
[16] Award ¶ 138.

refers that claim exclusively to another forum, unless there are good reasons (such as *force majeure*) preventing the claimant from complying with its contract. This issue is considered as a matter of admissibility, rather than jurisdiction.

In his Dissenting Opinion, Professor Crivellaro contended that SGS's claim that the Philippines violated Article X(2) of the BIT "seemed to me fully admissible before our Tribunal, without first being processed before the domestic courts as to *quantum* matters."[17] As the Tribunal's jurisdiction derives from Article X(2) of the BIT, Professor Crivellaro saw no reason why the Tribunal could not adjudicate the merits of the payment claim, including quantum: "our Tribunal has stated to have jurisdiction over both types of claims, whether founded on alleged breaches of the BIT or on alleged breaches of the contract, and I think it was mandated to proceed to examining the future Claimant's statements of claim and the Respondent's statements of defence concerning the substance of the dispute."[18]

(f) Is there a BIT claim independent of the CISS Agreement? (paras. 156-164)

The Tribunal characterized the present dispute as a dispute about the amount of money owed under a contract. No question of a breach of the BIT independent of a breach of contract claim was raised (as, arguably, in *SGS v. Pakistan*) and there was no allegation of a conspiracy by local officials to frustrate the investment. Rather, the unresolved issues between the parties, as presented to the Tribunal by SGS, concerned the determination of the amount still payable.

The Tribunal reasoned that SGS had failed to make out a case of expropriation: "[w]hatever debt the Philippines may owe to SGS still exists; whatever right to interest for late payment SGS had it still has."[19] The Tribunal noted that there has been no law or decree enacted by the Philippines attempting to expropriate or annul the debt, nor any action tantamount to an expropriation. The Tribunal emphasized:

> "A mere refusal to pay a debt is not an expropriation of property, at least where remedies exist in respect of such a refusal. *A fortiori* a refusal to pay is not an expropriation where there is an unresolved dispute as to the

[17] Dissent, ¶ 11.
[18] Dissent, ¶ 13.
[19] Award ¶ 161.

amount payable."[20]

On the other hand, the Tribunal reasoned that "an unjustified refusal to pay sums admittedly payable under an award or a contract at least raises arguable issues under [the fair and equitable treatment protection in] Article IV [of the BIT]."[21] Therefore, the Tribunal held that SGS had stated a fair and equitable treatment claim at the level of jurisdiction. But, the Tribunal ruled that it would be inappropriate and premature to decide on the claim in isolation from a decision by the chosen forum under the CISS Agreement (*i.e.,* the Philippine courts).

Accordingly, the Tribunal held that it had jurisdiction over SGS's claims under Articles X(2) and IV of the BIT, but that in respect of both provisions, SGS's claim was premature and must await the determination of the amount payable in accordance with the contractually agreed process.

(g) The retrospectivity issue (paras. 165-168)

The Tribunal concluded that SGS's claims under Articles X(2) and IV of the BIT, in association with Article VIII(2) of the BIT, fall within the temporal scope of the BIT and are not excluded on the grounds of retrospectivity. The Tribunal therefore rejected the Philippines' argument that the Tribunal lacked jurisdiction because the BIT does not apply retrospectively to claims which arose prior to its entry into force on April 23, 1999.

The Tribunal recalled that Article 28 of the Vienna Convention on the Law of Treaties provides that the substantive provisions of a BIT "do not bind a party in relation to any act or fact which took place or any situation which ceased to exist before the date of the entry into force of the treaty."[22] However, in international practice a different approach is taken to the application of treaties to procedural or jurisdictional clauses than to substantive obligations. The Tribunal held that "it is clear that [Article VIII of the BIT] applies to breaches which are continuing at that date, and the failure to pay sums due under a contract is an example of a

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[20] *Id.*

[21] Award ¶ 162.

[22] Award ¶ 166; *see also Mondev International Ltd. v. United States of America*, 6 ICSID Reports, 192, 209, ¶ 70 (2002).

continuing breach."[23]

As to Articles IV and X(2) of the BIT (which are substantive, not merely procedural provisions), the Tribunal found that it was clear that the failure to observe obligations arising under the CISS Agreement could not have occurred before the BOC made recommendations to the Secretary of Finance in 2001 as to the total amount payable under the CISS Agreement. This was well after the entry into force of the BIT, and there is no accordingly no problem of the retrospective application of the BIT in this case.

3. Decision

The Tribunal held that it has jurisdiction over the dispute pursuant to Article VIII(2) of the BIT, in combination with Articles X(2) and IV of the BIT. The Tribunal dismissed SGS's expropriation claims based on Article VI of the BIT.

A majority of the Tribunal held that SGS is bound by the terms of the exclusive jurisdiction clause in Article 12 of the CISS Agreement to establish the quantum or content of the obligation which, under Article X(2) of the BIT, the Philippines is required to observe. The majority therefore ruled that the arbitration proceedings should be stayed pending a decision on the amount due but unpaid under the CISS Agreement, a matter which (if not agreed by the parties) is to be determined by the agreed contractual forum under the CISS Agreement. The proceedings would resume on the request of either party once this condition for admissibility had been satisfied.

[23] Award ¶ 167.