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THE ROLE OF COUNTERCLAIMS IN REBALANCING INVESTMENT LAW

by
Andrea K. Bjorklund*

Examining investment treaty arbitration in isolation suggests an imbalance in both substance and procedure. Though international investment treaties are aimed at correcting the asymmetry that exists if states can exercise unchecked sovereign authority over investors, once a dispute starts, a new imbalance arises. Procedurally, most international investment agreements (IIAs) permit investors to commence claims against host states but do not contain a reciprocal right for the state to commence a claim against an investor. Substantively, most agreements impose obligations on states without imposing any obligations on investors. While states are obligated to abide by the terms of the agreement, and investors are implicitly (or sometimes explicitly) required to comply with host-state law, it is at best unclear whether states can submit counterclaims against investors when the substance of the investor-commenced dispute is a violation of an IIA. The core of an arbitral body's jurisdiction is the parties' consent to grant it authority over them. Thus, whether or not a counterclaim is possible depends on the breadth of an investor's consent at the commencement of the claim. Certain treaties might have broad enough dispute resolution clauses to encompass counterclaims, but most do not. While the arbitral rules most likely to govern investment treaty disputes envision counterclaims, reference to them is a slim reed on which to base an investor's consent. Moreover, counterclaims are intertwined with the law applicable to them, so that a state's ability to submit counterclaims must be accompanied by agreement about the tribunal's authority to apply that law. This Essay suggests that drafting treaties to permit closely related counterclaims would help to rebalance investment law by enabling both parties to bring all claims related to a dispute within a single tribunal's authority.

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INTRODUCTION

The ability of counterclaims to help rebalance investment law depends on whether and how investment law lacks equilibrium. The asymmetry in investment treaties is somewhat overstated—arguably the investment treaty helps to address the asymmetry that exists if a state can exercise its sovereign authority to change the playing field on which the investor is operating. The state sometimes does this in an unfair manner and without being held to account in its local courts, whether because of state immunity, bias in the local judiciary, a lack of separation of powers between the branches of government, or even some other cause.¹ To the extent that a state's actions are constrained by the investment treaty, the investment treaty can be viewed as righting an existing imbalance.² Yet, once the arbitration itself commences, new imbalances become apparent.

Examining the investment treaty arbitration in isolation suggests an imbalance in both substance and procedure. Procedurally, treaty arbitration is commenced when an investor submits a claim against a host state. States cannot submit claims under most investment treaties; the process must be commenced by the investor itself.³ As far as contract-based arbitration is concerned, disputes concerning contracts between the foreign investor and the host state might also be settled in arbitration so long as the parties consent;⁴ counterclaims by states, and even claims by states, will be possible in those cases.⁵ Absent any consent to arbitration, it is likely that the domestic side of the dispute, assuming there is one, will proceed in municipal courts with those proceedings governed by domes-

¹ See Charles N. Brower & Stephan W. Schill, *Is Arbitration a Threat or a Boon to the Legitimacy of International Investment Law?*, 9 CHI J. INT'L L. 471, 476–78 (2009).

² There is a great deal of concern about regulatory “chill” effected by international investment agreements, but documented instances are rare. *E.g.*, Jean E. Kalicki, *Counterclaims by States in Investment Arbitration*, INVESTMENT TREATY NEWS (Jan. 14, 2013), <http://www.iisd.org/itm/2013/01/14/counterclaims-by-states-in-investment-arbitration-2>; see also Barnali Choudhury, *Recapturing Public Power: Is Investment Arbitration's Engagement of the Public Interest Contributing to the Democratic Deficit?*, 41 VAND. J. TRANSNAT'L L. 775, 778–79 (2008).

³ See Jan Paulsson, *Arbitration Without Privity*, 10 ICSID REV. 232, 232–34 (1995).

⁴ *Id.* at 234.

⁵ The question of the so-called “umbrella clause” will be addressed further below. See *infra* notes 39–43 and accompanying text.

tic law, while any investment treaty arbitration will proceed on a separate plane with those proceedings governed by international law.

Substantively, most international investment agreements (IIAs) impose obligations on states, but do not impose them on investors.⁶ Indeed, international law generally does not impose obligations directly on non-state entities.⁷ There may be requirements, both implicit and explicit, that an investor comply with host state laws,⁸ but rarely is there any express provision in the treaty permitting a state to challenge an investor for a failure to abide by those obligations, or for a state to submit any counterclaim at all.⁹ Indeed, many IIAs specifically limit the jurisdiction of tribunals to hear claims of violations of certain provisions of the treaty and explicitly require that there be a “measure”—a state act—to challenge.¹⁰ By definition this means that investors can submit claims against states, but states cannot submit counterclaims against investors when the substance of the dispute is a violation of an IIA.¹¹ These limitations are meant to circumscribe the power of an arbitral tribunal. In so doing, they may prevent the assertion of counterclaims, a somewhat ironic outcome in that this particular limitation of power is not necessarily desired by those who would otherwise support restraining the authority of investor-state arbitral tribunals.

Thus, it is certainly true that looking at investment treaty arbitration in isolation, the procedure is usually one-sided and that disequilibrium

⁶ JESWALD W. SALACUSE, *THE THREE LAWS OF INTERNATIONAL INVESTMENT: NATIONAL, CONTRACTUAL, AND INTERNATIONAL FRAMEWORKS FOR FOREIGN CAPITAL* 383–84 (2013); Jason Webb Yackee, *Investment Treaties and Investor Corruption: An Emerging Defense for Host States?*, 52 VA. J. INT’L L. 723, 742 (2012).

⁷ There is of course an enormous amount of literature about this topic, particularly with reference to the Alien Tort Statute. See generally José E. Alvarez, *Are Corporations “Subjects” of International Law?*, 9 SANTA CLARA J. INT’L L. 1 (2011); William S. Dodge, *Investor–State Dispute Settlement Between Developed Countries: Reflections on the Australia–United States Free Trade Agreement*, 39 VAND. J. TRANSNAT’L L. 1 (2006); Chimène I. Keitner, *Conceptualizing Complicity in Alien Tort Cases*, 60 HASTINGS L.J. 61 (2008); Peter Muchlinski, *Corporate Social Responsibility*, in *THE OXFORD HANDBOOK OF INTERNATIONAL INVESTMENT LAW* 637 (Peter Muchlinski et al. eds., 2008).

⁸ See, e.g., SALACUSE, *supra* note 6, at 366–74 (describing requirements for investments to be covered by treaties).

⁹ See Ana Vohryzek-Griest, *State Counterclaims in Investor–State Disputes: A History of 30 Years of Failure*, 15 INT’L LAW: REVISTA COLOMBIANA DE DERECHO INTERNACIONAL 83, 111–14 (2009). Examples of exceptional treaties that do address counterclaims may be found in the text accompanying notes 21 to 24, below.

¹⁰ See Paulsson, *supra* note 3, at 232–33, 255. See also text accompanying notes 21 to 22, below.

¹¹ Pierre Lalive & Laura Halonen, *On the Availability of Counterclaims in Investment Treaty Arbitration*, 2 CZECH Y.B. INT’L L. 141, 150–51 (2011); Vohryzek-Griest, *supra* note 9, at 86–87, 112, 114; Anne K. Hoffmann, *Counterclaims by the Respondent State in Investment Arbitrations: The Decision on Jurisdiction over Respondent’s Counterclaim in Saluka Investments B.V. v. Czech Republic*, 3 TRANSNAT’L DISP. MGMT., Dec. 2006, at 1, <http://www.transnational-dispute-management.com/article.asp?key=849>; Kalicki, *supra* note 2.

might be redressed by the ability of states to submit counterclaims against investors.¹² It might be said that, absent the ability to submit a counterclaim, a state cannot win; the most it can hope to do is not to lose. Moreover, although states are not without any ability to seek redress even absent the ability to submit counterclaims, the advantages to investment arbitration that investors appreciate, such as the enforceability of arbitral awards, might appeal to states as well.¹³

Notwithstanding the hurdles they face, states are becoming more aggressive in asserting counterclaims against investors, though their efforts have tended not to be successful.¹⁴ Yet there seems to be a growing interest in the phenomenon and given arbitral pronouncements that lead in varying directions, it is fair to say it is an unresolved issue.¹⁵ Of course,

¹² See, e.g., Andrea K. Bjorklund, *Improving the International Investment Law and Policy System: Report of the Rapporteur Second Columbia International Investment Conference: What's Next in International Investment Law and Policy?*, in *THE EVOLVING INTERNATIONAL INVESTMENT REGIME: EXPECTATIONS, REALITIES, OPTIONS* 213, 219–31 (José E. Alvarez et al. eds., 2011); U.N. CONFERENCE ON TRADE & DEV., *INTERNATIONAL INVESTMENT RULE-MAKING: STOCKTAKING, CHALLENGES AND THE WAY FORWARD*, at 75–76, U.N. Sales No. E.08.II.D.1 (2008).

¹³ There is no global judgments convention. Arbitral awards, include investment arbitral awards, are thus often viewed as more readily enforceable than court judgments because they fall under either the ICSID Convention or the New York Convention on Recognition and Enforcement of Arbitral Awards. See Andrea K. Bjorklund, *State Immunity and the Enforcement of Investor-State Arbitral Awards*, in *INTERNATIONAL INVESTMENT LAW FOR THE 21ST CENTURY: LIBER AMICORUM* CHRISTOPH SCHREUER 302, 305–08 (Christina Binder et al. eds. 2009). The tenacity with which investors resist counterclaims suggests that they would rather defend themselves in municipal courts than in international arbitration. It might also be simply litigation or arbitration strategy.

¹⁴ Vohryzek-Griest, *supra* note 9, at 86, 92–111.

¹⁵ Compare *Roussalis v. Romania*, ICSID Case No. ARB/06/1, Award, ¶¶ 871–76 (Dec. 7, 2011), <http://www.italaw.com/sites/default/files/case-documents/ita0723.pdf> (finding that the treaty did not grant the tribunal jurisdiction over the state counterclaim), *Saluka Invs. BV v. Czech Republic*, UNCITRAL Arb., Decision on Jurisdiction over the Czech Republic's Counterclaim, (May 7, 2004), http://www.pca-cpa.org/showfile.asp?fil_id=106 (finding that the state counterclaims were outside the tribunal's jurisdiction, but that the scope of the treaty in principle permitted certain counterclaims), and *Paushok v. Gov't of Mong.*, UNCITRAL Arb., Award on Jurisdiction and Liability, ¶¶ 694–98 (April 28, 2011), <http://italaw.com/documents/PaushokAward.pdf> (same), with *Roussalis v. Romania*, ICSID Case No. ARB/06/01, Declaration of W. Michael Reisman (Nov. 28, 2011), <http://italaw.com/sites/default/files/case-documents/ita0724.pdf> (disagreeing with the majority's rejection of counterclaims on the ground of absence of consent), and *Goetz v. Republic of Burundi*, ICSID Case No. ARB/01/2, Sentence, ¶¶ 282–85 (June 21, 2012), <http://www.italaw.com/sites/default/files/case-documents/italaw1086.pdf> (ICSID Convention Article 40 and ICSID Arbitration Rule 46 permit tribunal to hear counterclaims). In *Burlington v. Ecuador* the claimant and the respondent came to an agreement whereby the claimant agreed not to dispute the jurisdiction of the tribunal over Ecuador's counterclaims. *Burlington Resources, Inc. v. Republic of Ecuador*, ICSID Case No. ARB 08/5, Decision on Liability, ¶¶ 93, 174 (Dec. 14, 2012), http://www.italaw.com/sites/default/files/case-documents/italaw1094_0.pdf. The tribunal's disposition of the case obviated the need for it to consider the

even if a state cannot submit a counterclaim, allegations of improper behavior on the part of an investor might help a state defend itself from the investor's claims of fair and equitable treatment violations by demonstrating that the state's conduct was warranted because of the investor's actions. More controversial is whether a state can seek diminution of the damages awarded against it by arguing that they should be "set off" against damage caused by the investor.¹⁶ In both of those examples, however, the state can only seek to diminish the investor's rights; it cannot seek affirmative relief from the investor. The ability to submit counterclaims—most likely based on investor's alleged non-compliance with host state's domestic laws and regulations or its breach of an investment contract, where there was one—is thus appealing for states defending themselves in an investment arbitration."

Counterclaims show some promise as a means to rebalance investment law by bringing all claims related to the subject matter at hand within the purview of a single tribunal's authority. Yet the ability to submit claims must be accompanied by agreement about the law applicable to govern the investor's conduct and the arbitral tribunal's authority to apply that law. The law most likely to govern the investor's conduct is that of the host state, which raises the question of just how much authority an arbitral tribunal should have to apply different municipal laws, including public law.¹⁷ In redressing one imbalance one should not lose sight of a different question of balance—the allocation of authority between do-

counterclaims. *Id.*; see also James Crawford, *Treaty and Contract in Investment Arbitration*, 24 *ARB. INT'L* 351, 364–66 (2008); Hoffman, *supra* note 11, at 1, 10.

¹⁶ In the recent *Occidental Petroleum v. Ecuador* case, the tribunal reduced the damages awarded to Occidental on grounds of "contributory negligence." *Occidental Petroleum Corp. v. Republic of Ecuador*, ICSID Case No. ARB/06/11, Award, ¶¶ 670, 678–80 (Oct. 5, 2012), <http://www.italaw.com/sites/default/files/case-documents/italaw1094.pdf>.

¹⁷ There has been a good bit of debate about whether investment arbitration is a newly emergent global administrative law. See, e.g., Benedict Kingsbury, *The Concept of 'Law' in Global Administrative Law*, 20 *EUR. J. INT'L LAW* 23, 25 (2009); Stephan W. Schill, *Enhancing International Investment Law's Legitimacy: Conceptual and Methodological Foundations of a New Public Law Approach*, 52 *VA. J. INT'L L.* 57, 59 (2011). Whether investment tribunals can or should actually apply domestic administrative law raises another set of questions. The "public law taboo" used to prevent courts in one jurisdiction from enforcing the public laws of another; it has been eroded in recent years. See Felix D. Strebler, *The Enforcement of Foreign Judgments and Foreign Public Law*, 21 *LOY. L.A. INT'L & COMP. L.J.* 55, 119–23 (1999). The arbitral analogue is the question of "arbitrability"—those questions that cannot be entrusted to arbitrators due to their public nature. Those, too, have been limited over the years. See, e.g., *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 628–39 (1985); *Scherk v. Alberto-Culver Co.*, 417 U.S. 506, 513 (1974). This concern was highlighted by the tribunal in *Paushok v. Mongolia*: "Thus, if the Arbitral Tribunal extended its jurisdiction to the Counterclaims, it would be acquiescing to a possible exorbitant extension of Mongolia's legislative jurisdiction without any legal basis under international law to do so, since the generally accepted principle is the non-extraterritorial enforceability of national public laws and, specifically, of national tax laws." *Paushok*, *supra* note 15, ¶ 695.

mestic courts and international tribunals. Giving investor–state tribunals the authority to hear counterclaims may alter that balance of power as well; whether that is a reasonable trade-off depends on one’s view of the importance of preserving the jurisdiction of and encouraging recourse to local courts and tribunals. An allocation of authority to hear different claims based on relative expertise while ensuring adequate communication between the respective dispute settlement bodies might more reasonably permit the consideration of the investor’s conduct in light of domestic law.

This Essay first explores the bases for an investment tribunal’s authority to hear counterclaims under the current investment law regime. It then explores the advantages and disadvantages of bringing counterclaims within the remit of investment tribunals. Finally, it concludes with the assessment that limited counterclaims will have to become part of the landscape if investor–state dispute settlement is to survive, though that will probably take state activity as drafters of treaties as well as state activity as defendants in investor–state disputes.

I. BASIS FOR TRIBUNAL AUTHORITY TO HEAR COUNTERCLAIMS

The ability of a state to assert a counterclaim will depend on whether or not the investor has consented to arbitrate counterclaims against it.¹⁸ Arbitration is a creature of consent; the tribunal draws its authority from the agreement of the parties to submit certain claims to it. The investment agreement is generally held to contain a unilateral offer of consent on the part of the host state which is accepted by the other disputing party, the investor or, in some cases, the investment itself, by instituting the arbitration proceedings.¹⁹

A. *Treaty Provisions*

The breadth of the investor’s consent (i.e. whether it encompasses counterclaims) and the related question of whether the tribunal will have jurisdiction over counterclaims, will depend first on the treaty’s language regarding the scope of investor–state dispute settlement (ISDS).²⁰

¹⁸ CHRISTOPH H. SCHREUER ET AL., *THE ICSID CONVENTION: A COMMENTARY* 106, 751–52 (2009).

¹⁹ *Id.* at 211–12; see Paulsson, *supra* note 3, at 233–34.

²⁰ It has even been said that if “a general principle can be discerned from [the practice of multiple international tribunals adopting procedural rules for the adjudication of counterclaims], it is that the jurisdiction *ratione materiae* of an international tribunal extends to counterclaims unless expressly excluded by the constitutive instrument.” ZACHARY DOUGLAS, *THE INTERNATIONAL LAW OF INVESTMENT CLAIMS* 256 (2009). My assessment is that this goes too far; while it is true that most international tribunals have procedural rules permitting counterclaims, those provisions do not address whether or not there has been consent to the counterclaim in any given case.

A very few treaties explicitly address counterclaims. The Common Market for Eastern and Southern Africa (COMESA) Investment Agreement (2007) provides in Article 28(9):

A Member State against whom a claim is brought by a COMESA investor under this Article may assert as a defence, counterclaim, right of set off or other similar claim, that the COMESA investor bringing the claim has not fulfilled its obligations under this Agreement, including the obligations to comply with all applicable domestic measures or that it has not taken all reasonable steps to mitigate possible damages.²¹

Notably, the part of the COMESA Agreement that sets out the general substantive obligations also includes a general obligation of investors to comply with domestic laws: “COMESA investors and their investments shall comply with all applicable domestic measures of the Member State in which their investment is made.”²²

IAs frequently refer to compliance with domestic laws at the stage of making the investment, yet the COMESA Agreement explicitly extends this obligation to the post-establishment phase.²³ The general obligation of investors to comply with national law is thereby raised to the international treaty level. This, in turn, puts it on an equal footing with the obligations of the host state and thereby gives jurisdiction over the possible counterclaims to an investment tribunal constituted under the treaty.²⁴

²¹ Investment Agreement for the COMESA Common Investment Area art. 28(9), May 22–23, 2007, available at <http://vi.unctad.org/files/wksp/iiaawksp08/docs/wednesday/Exercise%20Materials/invagreecomesa.pdf>.

²² *Id.* art. 13. Recent Indian bilateral investment treaties (BITs) include a provision that goes in the same direction as the COMESA Agreement. Article 12 of the India–Nepal BIT states: “Except as otherwise provided in this Agreement, all investments shall be governed by the laws in force in the territory of the Contracting Party in which such investments are made.” Agreement for the Promotion and Protection of Investments, India–Nepal, art. 12(1), Oct. 21, 2011, available at http://unctad.org/sections/dite/iia/docs/bits/India_Nepal.pdf. The India–Slovenia BIT contains the same language. Agreement on the Mutual Promotion and Protection of Investments, India–Slovn., art. 15(1), June 14, 2011, available at http://unctad.org/sections/dite/iia/docs/bits/India_Slovenia.pdf.

²³ Investment Agreement for the COMESA Common Investment Area, *supra* note 20, art. 13. Those pre-establishment provisions have not served as the basis for a counterclaim, but have been considered by tribunals as relevant to the question of whether an investor could sustain its claim under the investment treaty. *Fraport AG Frankfurt Airport Servs. Worldwide v. Republic of the Phil.*, ICSID Case No. ARB/03/25, Award, ¶¶ 401, 402 (Aug. 16, 2007), <http://italaw.com/documents/FraportAward.pdf>; *Inceysa Vallisoletana, S.L. v. Republic of El Sal.*, ICSID Case No. ARB/03/26, Award, ¶¶ 208, 332 (Aug. 2, 2006), http://italaw.com/documents/Inceysa_Vallisoletana_en_001.pdf.

²⁴ Presumably investors have a duty to comply with host state law at the commencement of an investment and throughout its maintenance of activities in the state even in the absence of treaty clauses referring to host state law; this obligation is imposed on investors by the international law principle of territorial sovereignty. 2 SAMUEL PUFENDORF, *DE JURE NATURAE ET GENTIUM* 403 (C.H. & W.A. Oldfather, trans., Oceana Pubs. 1934) (1688). The question is whether a failure to comply with

Absent an explicit clause, one has to look at the treaty provisions that might have some bearing on the matter. Some ISDS provisions are quite broad and confer on tribunals the authority to hear any “dispute between an investor of one Contracting Party and the other Contracting Party in connection with an investment,” or some similar formulation.²⁵ Such a clause appears to be more conducive to counterclaims compared to narrow ISDS clauses that limit arbitrable claims to those alleging the breach of a treaty provision.²⁶ Under NAFTA Chapter 11, for example, investors of a party are entitled to:

submit to arbitration under this Section a claim that another Party has breached an obligation under:

(a) Section A or Article 1503(2) (State Enterprises), or

(b) Article 1502(3)(a) (Monopolies and State Enterprises) . . . ,

and that the investor has incurred loss or damage by reason of, or arising out of, that breach.²⁷

Because the referenced sections of NAFTA do not impose obligations on investors, that latter formulation makes the argument that a treaty confers jurisdiction on a tribunal to hear a counterclaim difficult. Indeed, based on this argument, the tribunal in *Roussalis v. Romania* refused to entertain counterclaims against the foreign investor.²⁸

It is worth remembering that a counterclaim is in effect a claim; it would be odd should a state be capable of filing a counterclaim if it could not have filed a claim.²⁹ Yet it seems possible that the NAFTA parties left open that possibility. Notwithstanding the limiting language in NAFTA Article 1116, Article 1137(3) states: “In an arbitration [regarding receipts under insurance or guarantee contracts], a Party shall not assert, as a defense, counterclaim, right of setoff or otherwise”³⁰ Arguably it makes no sense to specifically preclude counterclaims in one circumstance un-

those laws is actionable on the international plane and whether an investor-state dispute settlement tribunal has the authority to issue a ruling with respect to any alleged violations.

²⁵ *E.g.*, Agreement for the Promotion and Protection of Investments, art. 9(1), India-Neth., Nov. 6, 1995, available at <http://finmin.nic.in/bipa/Netherlands.pdf>; see also DOUGLAS, *supra* note 20, at 234, 257.

²⁶ DOUGLAS, *supra* note 20, at 257.

²⁷ North American Free Trade Agreement, art. 1116, Dec. 17, 1992, 32 I.L.M. 605, 642-43 (1993) [hereinafter NAFTA].

²⁸ *Roussalis*, Award, *supra* note 15, at ¶¶ 871-76; Professor Michael Reisman disagreed with the conclusion of the majority. *Roussalis*, Declaration of W. Michael Reisman, *supra* note 14. For a general review of treaty practice, see U.N. CONFERENCE ON TRADE & DEV., DISPUTE SETTLEMENT: INVESTOR-STATE (2d ed. forthcoming 2013).

²⁹ Vohryzek-Griest, *supra* note 9, at 112.

³⁰ NAFTA, *supra* note 27, art. 1137(3).

less they were permitted in others.³¹ Yet this might also have been an excess of zeal on the part of NAFTA's drafter to ensure that an investor's recovery should not be limited by other sources of compensation available to investors.³²

Professor Douglas makes the interesting point that extending a tribunal's jurisdiction to encompass counterclaims in a treaty such as NAFTA Chapter 11 would result in an inequality whereby a host state could submit counterclaims "based upon a contractual obligation (if there is an investment agreement in place between the investor and the host state) a tort, unjust enrichment, or a public law act, in circumstances where the investor's primary claims are limited to breaches of Chapter 11 obligations."³³ In such a case, he concludes that "it would be preferable to construe Chapter 11 of NAFTA as excluding the possibility of counterclaims by the host state respondent."³⁴

The applicable law clause in a treaty might also be relevant to the availability of a counterclaim. Some treaties direct tribunals to apply the treaty itself (and relevant international law),³⁵ whereas others designate the domestic law of the host state as one of the sources of applicable law.³⁶ In the former case, it is less clear that a state could submit claims against the investor as it is unlikely to have obligations under the treaty or international law.³⁷ In the latter case, allegations of breaches of host state law might more readily be brought before the investment tribunal. It is possible to argue that the tribunal's authority to apply international law includes its ability to apply international conflict-of-laws rules to select the appropriate law, and that in most cases the law applicable to the conduct of the investor would be host state law.³⁸ Thus, the tribunal would have

³¹ See Helene Bubrowski, *Balancing IIA Arbitration Through the Use of Counterclaims*, in *IMPROVING INTERNATIONAL INVESTMENT AGREEMENTS* 212, 222 (Armand de Mestral & Céline Lévesque eds., 2013).

³² MEG N. KINNEAR, ANDREA K. BJORKLUND & JOHN F.G. HANNAFORD, *INVESTMENT DISPUTES UNDER NAFTA: AN ANNOTATED GUIDE TO NAFTA CHAPTER 11*, at 1137.7–1137.8 (2006, 2009 update).

³³ DOUGLAS, *supra* note 20, at 257.

³⁴ *Id.*

³⁵ ANDREW NEWCOMBE & LLUÍS PARADELL, *LAW AND PRACTICE OF INVESTMENT TREATIES: STANDARDS OF TREATMENT* 82 (2009).

³⁶ *Id.* at 79.

³⁷ It is possible to argue that investors do have international law obligations. Often, though not always, these are grounded in soft law. See Keitner, *supra* note 7; Muchlinski, *supra* note 7. For a creative theory about obligations grounded in custom and general principles, see, for example, Yaraslau Kryvoi, *Counterclaims in Investor-State Arbitration* 21–24 (London Sch. of Eco. Law Dep't, LSE Law, Soc'y & Econ. Working Paper 8/2011), available at <http://ssrn.com/abstract=1891935>.

³⁸ See MONIQUE SASSON, *SUBSTANTIVE LAW IN INVESTMENT TREATY ARBITRATION: THE UNSETTLED RELATIONSHIP BETWEEN INTERNATIONAL LAW AND MUNICIPAL LAW* 194, 206–08 (2010); Emmanuel Gaillard & Yas Banifatemi, *The Meaning of "and" in Article 42(1), Second Sentence, of the Washington Convention: The Role of International Law in the ICSID Choice of Law Process*, 18 ICSID REV. 375, 379–81 (2003); W. Michael

the authority to apply the domestic law of the host state regardless of whether the investor's duty to comply with domestic law is mentioned in the treaty. In such a case, though, the hurdle of consent might be that much more difficult to overcome.

Another textual hook for a counterclaim is an "observance of undertakings" clause, also called an "umbrella" clause.³⁹ Umbrella clauses have been interpreted to transform a claim that a government has breached the terms of a contract it has with a foreign investor into a claim that the state has breached a treaty obligation.⁴⁰ This is because a failure to honor the contract is also a failure to honor the guarantee made by the state in the treaty. An investment treaty tribunal hearing a claim brought under the umbrella clause will effectively be hearing a breach of contract claim,⁴¹ which suggests counterclaims with respect to the contract would appropriately be heard as well. Yet if the scope of the treaty reached only claims that there was a breach of the treaty, one could argue that the tribunal's jurisdiction encompasses the umbrella clause claim only to the extent it involved a breach by the state. This argument is more compelling depending on the outcome of the umbrella clause argument: if there is a parallel case in which the contract-based claims are being heard, that tribunal would hear counterclaims.⁴² If, however, the investment tribunal effectively took control of all contract-based claims, the tribunal should be able to hear counterclaims as well.⁴³

Reisman, *The Regime for Lacunae in the ICSID Choice of Law Provision and the Question of Its Threshold*, 15 ICSID REV. 362, 373–74 (2000).

³⁹ A typical umbrella clause is one found in Article 2.2 of the Bahrain–Turkmenistan BIT: "Each Contracting Party shall observe any obligation it may have entered into with regard to investments of investors of the other Contracting Party." Agreement for the Promotion and Protection of Investments, Bahr-Turkm., art. 2.2, Feb. 9, 2011, http://www.unctad.org/sections/dite/iaa/docs/bits/Bahrain_Turkmenistan.pdf.

⁴⁰ See SASSON, *supra* note 38, at 175.

⁴¹ See NEWCOMBE & PARADELL, *supra* note 35, at 451.

⁴² Preserving the formal distinction between treaty-based claims and contract-based claims by allocating authority to different tribunals allows a cleaner distinction between these two. In practice, however, the investment tribunal might have to consider alleged contractual breaches, including both claims and counterclaims, in order to determine whether there had been a breach of the treaty. "In doing so, the Tribunal would in no way be exercising jurisdiction over the contract, it would simply be taking into account the parties behaviour under and in relation to the terms of the contract in determining whether there has been a breach of a distinct standard of international law . . ." *Compañía de Augas del Aconquija S.A. v. Argentine Republic*, ICSID Case No. ARB/97/3, Award, ¶ 7.3.10 (Aug. 20, 2007), <http://www.italaw.com/sites/default/files/case-documents/ita0215.pdf>.

⁴³ The *SGS v. Pakistan* tribunal noted the importance of assuring that the investor could not foreclose the State's ability to submit a claim: "It would be inequitable if, by reason of the invocation of ICSID jurisdiction, the Claimant could on the one hand elevate its side of the dispute to international adjudication and, on the other, preclude the Respondent from pursuing its own claim for damages by obtaining a stay of those proceedings for the pendency of the international proceedings, if such international proceedings could not encompass the Respondent's claim." *SGS Société Générale de Surveillance S.A. v. Islamic Republic of Pak.*, ICSID Case No.

In one recent case two of the counterclaims were directed towards the claimant's conduct in using investor-state arbitration: one was "malicious prosecution (abuso del derecho);" the second was a breach of the concession contract which involved a "waiver of the right to use diplomatic or consular channels."⁴⁴ Each was denied on the merits, without discussion of the permissibility of the claims themselves.⁴⁵ It is an interesting question whether such claims could be viewed as impliedly available should a claimant in fact abuse the process, regardless of treaty language limiting claims or claimants.⁴⁶

B. *Reference to Counterclaims in Other Documents*

Investment treaties do not contain full-fledged rules of arbitral procedure. While some, such as the agreements entered into by Canada and the United States, contain rather detailed procedural specifications, even those treaties list the relevant arbitral rules under which investors may choose to submit their claims. Investors most commonly seek arbitration pursuant to the ICSID Convention and its accompanying arbitral rules or pursuant to the UNCITRAL Arbitration Rules. Thus, one possible source of a tribunal's authority to hear counterclaims is the arbitration's procedural rules.

1. *Arbitration Under the ICSID Convention*

The ICSID Convention foresees the possibility of counterclaims in Article 46:

Except as the parties otherwise agree, the Tribunal shall, if requested by a party, determine any incidental or additional claims or counter-claims arising directly out of the subject-matter of the dispute provided that they are within the scope of the consent of the parties and are otherwise within the jurisdiction of the Centre.⁴⁷

One possible interpretation is that arbitrations submitted under the ICSID Convention by a disputing investor arguably encompass this provision and permit the filing of counterclaims by a host state.⁴⁸ Under this

ARB/01/13, Procedural Order No. 2 (Oct. 16, 2002), 18 ICSID Review 294, 302–03 (2003).

⁴⁴ *Occidental*, *supra* note 16, ¶ 854.

⁴⁵ *Id.* ¶¶ 856–60. The claimant had questioned whether the doctrine of abuse of process had any place at all in international arbitration. *Id.* ¶ 288.

⁴⁶ Abuse of process might well result in costs awards against the abuser, whether or not it provides a basis for a substantive claim. *Vohryzek-Griest*, *supra* note 9, at 110 (referring to *Maritime Int'l Nominees Establishment v. Republic of Guinea*, ICSID Case No. ARB/84/4, Award, § 10(a) (Jan. 6, 1988), 4 ICSID Rep. 61 (1997)).

⁴⁷ Convention on the Settlement of Investment Disputes Between States and Nationals of Other States, art. 46, Mar. 18, 1965, 17 U.S.T. 1270, 1286, 575 U.N.T.S. 159 [hereinafter ICSID Convention]. For a discussion of these conditions, see SCHREUER, *supra* note 18, at 731–56.

⁴⁸ The applicable law provision of the ICSID Convention is found in Article 42 and directs a tribunal to apply "the law of the Contracting State party to the dispute

line of argument, Article 46 would expand or otherwise be considered an integral part of the treaty-based consent to arbitration, such that any submission of a claim to arbitration under the ICSID Convention would be deemed to permit a counterclaim. Yet it is also possible to view this provision as a procedural mechanism that would permit the filing of counterclaims only to the extent they would be encompassed by the consent instrument itself (keeping in mind that the ICSID Convention was negotiated when the expectation was that most cases brought to the Centre would be contract, not treaty, cases⁴⁹). Indeed, this difference of opinion was the basis of Professor Michael Reisman's dissent in the *Roussalis* case:

I understand the line of [the majority's] analysis but, in my view, when the States Parties to a [bilateral investment treaty] contingently consent, *inter alia*, to ICSID jurisdiction, the consent component of Article 46 of the Washington Convention is *ipso facto* imported into any ICSID arbitration which an investor then elects to pursue. It is important to bear in mind that such counterclaim jurisdiction is not only a concession to the State Party: Article 46 works to the benefit of both respondent state *and* investor. In rejecting ICSID jurisdiction over counterclaims, a neutral tribunal—which was, in fact, selected by the claimant—perforce directs the respondent State to pursue its claims in its own courts where the very investor who had sought a forum outside the state apparatus is now constrained to become the defendant.⁵⁰

Professor Reisman's frustration at the apparent absurdity of the result is understandable. Yet it seems the investor itself did not want to bring the counterclaim within the purview of the investment arbitration and was willing to be constrained to become a defendant in local courts, or it would not have fought the assertion of the counterclaim.⁵¹ This might, of course, have been a strategic decision on the part of the investor, and reading the investor's consent more broadly would have prevented the investor from avoiding the forum in which an award might be more readily enforceable.

(including its rules on the conflict of laws) and such rules of international law as may be applicable." ICSID Convention, *supra* note 47, art. 42.

⁴⁹ NEWCOMBE & PARADELL, *supra* note 35, at 44; ANTONIO R. PARRA, THE HISTORY OF ICSID 24–25, 132–35 (2012); Kalicki, *supra* note 2, at 2 (noting "Article 46's own reference to 'within the scope of consent' as an *extrinsic* precondition to the tribunal's hearing counterclaims"). Kalicki goes on to explain that "if Article 46 itself provided that consent, then its incorporated requirement of consent ('provided they are within the scope of consent') would be entirely circular and extraneous." *Id.* at 2.

⁵⁰ *Roussalis*, Declaration of W. Michael Reisman, *supra* note 15.

⁵¹ In *Burlington v. Ecuador* the parties came to an agreement that the tribunal could hear Ecuador's counterclaims. *Burlington Resources, Inc.*, *supra* note 15, ¶¶ 93, 174.

2. *Non-ICSID Arbitration Rules*

In addition to the ICSID Convention itself, most of the procedural rules that frequently govern investment treaty arbitrations contain provisions on the submission of counterclaims.⁵² If invoking arbitration under the ICSID Convention could be deemed to indicate consent to counterclaims due to the presence of Article 46, it might by analogy be possible to invoke the provisions in those sets of rules as well.

For example, the 1976 UNCITRAL Arbitration Rules provide that a “respondent may make a counter-claim arising out of the same contract or rely on a claim arising out of the same contract for the purpose of a set-off.”⁵³ The 2010 UNCITRAL Arbitration Rules provide that a tribunal may hear counterclaims provided the tribunal has jurisdiction over them.⁵⁴ The main questions regarding counterclaims thus relate to consent and the scope of a tribunal’s jurisdiction. This tends to place the question squarely back into an interpretation of the consent document—the investment treaty itself. Indeed, the revisions to the UNCITRAL Rules strongly suggest that the rules themselves are not a source of consent to the filing of counterclaims, but that the consent must be found elsewhere.

C. *Arbitral Practice*

As so often happens in cases of ambiguity or lacunae in the treaty, tribunals have come to different conclusions regarding the possibility of counterclaims, although the majority indicate some receptivity. Cases to date, which are still few, might be grouped into two categories. The first, exemplified by the majority in *Roussalis*, suggest that investor consent to counterclaims must be found in the investment treaty itself; consent cannot be implied from the procedural provisions referring to counterclaims in the applicable arbitral rules.⁵⁵ The second category suggests that in appropriate cases a claimant’s consent can be implied from the appli-

⁵² See, e.g., ICC Rules of Arbitration art. 5(5) (2012); London Court of Int’l Arbitration Rules art. 2.1(b) (1998); Stockholm Chamber of Com. Arbitration Rules art. 24(2)(iv) (2010); UNCITRAL Arbitration Rules, art. 21(3) (2010).

⁵³ UNCITRAL Arbitration Rules, art. 9(3) (1976), available at <http://www.uncitral.org/pdf/english/texts/arbitration/arb-rules/arb-rules.pdf>. Douglas suggests that under the old UNCITRAL rules the term “contract” is equivalent to “investment” and that a tribunal’s jurisdiction over primary claims and counterclaims can be achieved by interpreting contract to be equivalent to investment. DOUGLAS, *supra* note 20, at 259.

⁵⁴ UNCITRAL Arbitration Rules, *supra* note 53, art. 21(3).

⁵⁵ *Roussalis*, *supra* note 15, ¶¶ 869–77. It should be noted that the BIT in *Roussalis* had a narrower dispute resolution clause which referred to disputes concerning an obligation of the state; the Belgium–Burundi BIT in *Goetz v. Burundi* had a slightly broader clause and also an applicable law clause referring to municipal law as well as international law. Convention Concerning the Reciprocal Promotion and Protection of Investments, Belg. Lux. Econ. Union–Burundi, art. 8, ¶¶ 1, 5 Apr. 13, 1989, 1957 U.N.T.S. 439.

cable rules and their references to counterclaims, so long as the counterclaims have a close association with the allegations of treaty breach and no other barriers come into play. Thus, in *Saluka Investments B.V. v. Czech Republic*, the Czech Republic's advance of a counterclaim against the investor was not permitted because the specific agreement between the Czech Republic and Saluka anticipated arbitration under different rules in the event of a dispute⁵⁶ (thus negating any suggestion that the investor had consented to the treaty tribunal's jurisdiction to hear the counterclaim based on the contract) and because the counterclaim was not closely connected to the allegations regarding breaches of the investment protection rules (thus falling outside the tribunal's jurisdiction).⁵⁷ Notwithstanding these caveats, the *Saluka* tribunal made clear that the scope of the treaty, which reached any disputes relating to investments, permitted counterclaims in principle, so long as they were closely affiliated.⁵⁸ The *Goetz v. Burundi* tribunal came to a similar conclusion, as did the tribunal in *Paushok v. Mongolia*. The latter decision highlights the link between counterclaims and applicable law; one of the counterclaims would have been based on Mongolian tax laws, which the tribunal found outside its authority due to the public law taboo on the extraterritorial enforcement of tax awards, as opposed to on contractual claims, which the tribunal would have considered.⁵⁹

The agreement on the submission of counterclaims in *Burlington* highlights the importance of party consent.⁶⁰ *Ab initio*, the tribunal's decision with respect to counterclaims hinges on the authority given it by the treaty and by an investor's consent to arbitrate according to the terms of the treaty. The tribunal's authority thus depends on what the treaty parties negotiated—what terms the treaty parties made it possible for the investor to accept, and what terms they required the investor to accept to initiate arbitration. Professor Crawford emphasizes that the agreement between the investor and the state to arbitrate a claim is a contract that is bred by a treaty.⁶¹ Whether and how much parties can amend that contract to enlarge the tribunal's is an interesting question—the ICSID Con-

⁵⁶ *Saluka*, *supra* note 11, ¶¶ 56–58.

⁵⁷ *Id.* ¶¶ 76–80; *cf.* *Perenco Ecuador, Ltd. v. Republic of Ecuador*, ICSID Case No. ARB/08/6, Decision on Jurisdiction, ¶ 71 (June 30, 2011), https://icsid.worldbank.org/ICSID/FrontServlet?requestType=CasesRH&actionVal=showDoc&docId=DC2191_En&caseId=C301; *Paushok*, *supra* note 15, ¶ 694.

⁵⁸ *Saluka*, *supra* note 11, ¶ 39. The tribunal in *Paushok v. Government of Mong.* came to the same conclusion. *Paushok*, *supra* note 15, ¶¶ 684–99.

⁵⁹ *Paushok*, *supra* note 15, at ¶¶ 694–95.

⁶⁰ In *Occidental v. Ecuador* there did not appear to be consent to the tribunal's consideration of counterclaims, but there was no discussion of the tribunal's jurisdictional authority as the claims were readily dismissed on the merits. *Occidental*, *supra* note 16, ¶¶ 854–69.

⁶¹ Crawford, *supra* note 15, at 361.

vention might pose limits, for example.⁶² Nothing would seem to prevent the parties from entering into a parallel contract, but the intersection between that contract and the “BIT” contract might raise questions both similar to and different from the relationship between a contract arbitration and an investment arbitration that one finds in the umbrella clause cases.⁶³

II. BENEFITS OF COUNTERCLAIMS

Those tribunals that have at least in principle approved the filing of some counterclaims have recognized that bringing related claims together into the same case has several benefits. For the sake of ease I have categorized these into three groups; there could well be some overlap between the different sets of benefits.

Procedural Efficiency. Procedural efficiency would presumably be enhanced by permitting governments to submit counterclaims. Complex facts developed through the course of arbitrating the treaty-based claim would be relevant for the likely domestic law-based claims as well. A one-stop-shop for all claims related to the same cluster of events would encourage efficient decision-making with the arbitrators well informed about all relevant facts. It would also facilitate the assessment of damages and the calculation of countervailing damages. Having one set of counsel and one hearing would also streamline the process and minimize the duplication of expenses.⁶⁴

In addition, awards rendered by international arbitral tribunals are subject to enforcement under the applicable treaties. ICSID Convention awards are enforceable under the ICSID Convention;⁶⁵ virtually all other awards are enforceable under the New York Convention on Recognition

⁶² The dispute would still need to fall within the jurisdiction of the Centre. Given the status that contracting parties must afford to ICSID Convention awards, attempts to expand an arbitration to encompass tax matters, as in *Paushok v. Mongolia*, would put the contracting states in the position of having to enforce an award that they might well view as contravening public policy. This concern does not arise in non-ICSID Convention cases, because the states party to the New York Convention can refuse to enforce an award if it contravenes the public policy of the forum.

⁶³ One’s conception of the relationship between the home state and the investor might limit the investor’s freedom of action as well, at least if it could be viewed as intruding on the home state’s rights or affecting its obligations. The home state might be viewed as having negotiated protections for its investor that the investor should not readily jettison. Professor Douglas’s observation that a NAFTA arbitration could become unbalanced should a state be able to submit broad counterclaims while an investor can submit only limited claims illustrates what home states presumably did not want to happen. See the text accompanying notes 33 to 34, *supra*.

⁶⁴ Jean Kalicki has noted that allowing counterclaims “may lead to efficiency, to the centralization of inquiry and the avoidance of duplication.” Kalicki, *supra* note 2, at 1. It may also avoid anti-suit injunctions, anti-anti-suit injunctions, and the like. *Id.* at 1–2.

⁶⁵ ICSID Convention, *supra* note 47, art. 53.

and Enforcement of Arbitral Awards.⁶⁶ Enforceable awards include those rendered against investors.⁶⁷ Because arbitral awards are more readily enforceable than court judgments in most cases,⁶⁸ states might benefit from obtaining arbitral awards against investors much the same way that investors benefit from obtaining awards against host states.

Finally, permitting counterclaims might well discourage frivolous claims; it might also discourage states from raising frivolous objections.⁶⁹ If an investor has to take account of claims that might be filed against it, its zeal to file might diminish. The possibility of facing counterclaims might also have an effect on third-party funding decisions, as funders would have to assess the likelihood of affirmative liability in addition to the likelihood of success on the merits in the case against the opposing party. In short, the whole cost-benefit calculus would shift. The same is true for a respondent as well; if claims can be submitted only one way there is every incentive for a state to file jurisdictional objections to delay any hearing of the claim on the merits. Should the state be able to recover against the claimant, its willingness to move forward, at least when it has viable claims, would grow.

Legitimacy. Permitting governments to file counterclaims redresses concerns about the asymmetry of investor–state dispute settlement in which investors have both rights and remedies, whereas states have neither. Though one can readily argue that ISDS redresses the asymmetry that exists in its absence—a situation where states have sovereign power to act as they see fit and investors are often without redress due to poorly functioning, non-independent courts or state immunity rules or the like—it remains true that the spectacle of investors seeking multimillion or even billion dollar awards against host states with no reciprocal claim expected from the state raises questions about procedural and substantive fairness.⁷⁰ Moreover, states may want the opportunity to defend themselves and their reputations vigorously—to win, as opposed merely to “not lose.”

Counterclaims, especially if they were contractually based, might also shift the orientation of the proceedings towards private-law issues. Many have written about the administrative law, or even the constitutional law, nature of investment tribunals.⁷¹ Treaty obligations are meant to constrain the activities of states, so the emphasis on state behavior is not surprising. Contract-based counterclaims would enlarge those concerns to

⁶⁶ Convention on the Recognition and Enforcement of Foreign Arbitral Awards art. 1, June 10, 1958, 21 U.S.T. 2517, 2519, 330 U.N.T.S. 38.

⁶⁷ *Id.*; ICSID Convention, *supra* note 47, art. 53.

⁶⁸ See R. Doak Bishop, *Introduction: The Enforcement of Arbitral Awards Against Sovereigns*, in ENFORCEMENT OF ARBITRAL AWARDS AGAINST SOVEREIGNS 3–4 (R. Doak Bishop ed., 2009).

⁶⁹ See Kryvoi, *supra* note 37, at 4.

⁷⁰ See Bubrowski, *supra* note 31, at 214–15.

⁷¹ See Kingsbury, *supra* note 17, at 34–41; Schill, *supra* note 17, at 59.

assess the conduct of the investor and of its investment. This shift might serve to highlight and constrain undesirable investor conduct, thus improving corporate governance.

Enhance the Rule of Law. Permitting counterclaims makes it more possible that investors will be called to account for their actions. Though this can happen in the local courts in the place where the dispute is heard, those decisions sometimes lack force given perceptions about bias in the judiciary. A recent example of this phenomenon is *Chevron v. Ecuador*.⁷² Regardless of the merits of the case, what appear to be well-documented examples of procedural improprieties raise questions about the legitimacy of the \$18 billion award rendered against Chevron.⁷³ Had an international tribunal rendered the judgment there may well have been an outcry, yet the crux of the concerns would be different.

III. DRAWBACKS TO SUBMITTING COUNTERCLAIMS

As is so often (inevitably?) the case, the disadvantages might be viewed as the mirror-image of the advantages.

Procedural Inefficiency. The idealized picture of international arbitration as a speedy and efficient way to resolve international disputes has largely been debunked in both commercial and investment arbitration.⁷⁴ Enlarging the dispute to include counterclaims will simply accelerate this tendency. It will also likely raise issues related to the intersection between domestic and international dispute settlement. Ideally, treaty provisions such as “fork-in-the-road” clauses⁷⁵ would accommodate these concerns by requiring any actions in the local court to cease once an investor–state dispute claim is filed, if the investor-state claim is going to include claims that would replicate local procedures.

Other procedural problems and issue involve issues such as privity of contract. Against whom can the counterclaim be filed? Against the investor submitting the claim under the treaty, or against the investor’s investment, or both? The claimant is usually the investor submitting a claim on behalf of its investment, yet the counterclaim would often be submitted against the investment as the entity doing business in the host state’s

⁷² *Chevron Corp. v. Republic of Ecuador*, PCA Case No. 2009-23, UNCITRAL Arb, http://www.pca-cpa.org/showpage.asp?pag_id=1408.

⁷³ Christopher A. Whytock & Cassandra Burke Robertson, *Forum Non Conveniens and the Enforcement of Foreign Judgments*, 111 COLUM. L. REV. 1444, 1447–48 (2011); see also Lise Johnson, *Case Note: How Chevron v. Ecuador is Pushing the Boundaries of Arbitral Authority*, INVESTMENT TREATY NEWS (Apr. 13, 2012) <http://www.iisd.org/itn/2012/04/13/case-note-how-chevron-v-ecuador-is-pushing-the-boundaries-of-arbitral-authority/>.

⁷⁴ See, e.g., John Yukio Gotanda, *An Efficient Method for Determining Jurisdiction in International Arbitrations*, 40 COLUM. J. TRANSNAT’L L. 11, 12–13 (2001).

⁷⁵ For more information on fork-in-the-road clauses, see Laura Henry, *Investment Agreement Claims Under the 2004 Model U.S. BIT: A Challenge for State Police Powers?*, 31 U. PA. J. INT’L L. 935, 985 (2010).

jurisdiction and thus subject to its laws; that is often the entity with whom any concession contract is made as well. In such cases can the counterclaim effectively be submitted against the investor, and would the investor be liable to pay damages?⁷⁶

One might have assignment and delegation questions on the submission side as well. Can the federal government submit a counterclaim on behalf of all subnational governmental units, or on behalf of all government agencies? Attribution rules govern when a state can be liable for the acts of its constituents, yet they do not govern offensive uses of authority.⁷⁷ What law would govern that question? International law? Municipal laws governing the relationship between different branches of government and between state and local governments?

Illegitimacy. Permitting counterclaims is very likely to encourage the submission of counterclaims. In the first instance, this would likely aggrandize the power of ISDS tribunals who would be hearing more aspects of complex, multilayered disputes. For those concerned about the mechanism of ISDS itself, entrusting tribunals with the authority to hear counterclaims would possibly cement their status as alternatives to domestic courts, particularly if one took an expansive view of counterclaims. To the extent they would apply domestic public law, they might be grappling with an unfamiliar law in which they can claim no special expertise.⁷⁸ They would be yet one more step removed from the governmental process that enacted those laws and that might be able to act to correct any misapplication of the law.

Undermine the Rule of Law. One of the criticisms of ISDS has been its siphoning off from domestic courts disputes that might otherwise have been resolved locally.⁷⁹ Domestic courts then lose both the opportunity to exhibit their effectiveness and their ability to enhance their capacity to

⁷⁶ Sometimes it might be possible for a foreign-controlled investment itself to submit a claim (and Article 25(2)(b) of the ICSID Convention permits jurisdiction under the Convention to extend to disputes between an investment of a host state that is under foreign control). In those cases the privity issue would presumably not exist. See generally Kryvoi, *supra* note 37, at 10–11, 13–15.

⁷⁷ *Responsibility of States for Internationally Wrongful Acts*, [2001] 2[2] Y.B. Int'l L. Comm'n 20, arts. 4–11, U.N. Doc. A/CN.4/SER.A/2001/Add.1 (Part 2); Crawford, *supra* note 15, at 363 (“The second qualification is that there can only be contractual jurisdiction under a BIT in respect of an investment contract with the state itself, and not with a separate State entity having its own legal personality, and *a fortiori* with a third party. It is sometimes argued that the question is one of attribution under Chapter 2 of Part I of the ILC’s Articles on State Responsibility, but attribution has nothing to do with it. . . . The problem here concerns jurisdiction, not merits; the formation of a secondary agreement to arbitrate, not the breach of a primary obligation concerning the protection of investments.”).

⁷⁸ Kalicki, *supra* note 2, at 2.

⁷⁹ See U.N. CONFERENCE ON TRADE & DEV., *supra* note 28, at 8, 12, 33.

hear complex disputes.⁸⁰ To the extent that ISDS continues to be an attractive venue, or becomes an even more attractive venue, this problem will continue.

CONCLUSION

It is not surprising that a majority of the relatively few tribunals to have considered the question of counterclaims have at least in theory welcomed the possibility. As a matter of policy, on balance the advantages of permitting counterclaims outweigh the disadvantages, so long as they are narrowly drawn. Some efficiencies would almost certainly ensue. The procedural problems themselves are challenging but not decisive, and can be addressed through careful treaty drafting. More important is the question of legitimacy. As long as investor–state dispute settlement, viewed in isolation, is open to the charge of asymmetry, its bona fides will be subject to question.

The latter concern raised above—whether investment arbitration contributes to the rule of law and the relationship between investment tribunals and domestic courts—is the most vexing and the most troublesome. Permitting or encouraging investment treaty tribunals to hear multi-faceted disputes based on domestic public laws would likely to bring even more charges of illegitimacy, aggrandizement, and impingement on sovereignty against investment arbitration. Moreover, one has to consider what “equality of arms” should mean in the context of investment arbitration. Given that investment protections work to redress an asymmetry that exists without the investment treaty, altering investor-state dispute settlement to redress any imbalance within it should not go too far. As Professor Douglas has noted, permitting unlimited counterclaims while nonetheless observing limitations on claimants could generate inequality.⁸¹ Redressing an apparent imbalance in the investment treaty arbitration itself by effectively giving more authority to states might result in a return to the asymmetry that favors host states in the absence of treaty protections. Given that arbitral tribunals need to have a particular expertise in order to enhance their authority, tribunals should limit potential counterclaims to those closely connected to the dispute before the investment tribunal and grounded in law that the tribunal is capable of applying well. This limitation would enhance the prospects of greater efficiency and legitimacy while preserving a state’s authority to apply its public laws through its courts.

These are policy considerations, however, and a tribunal’s authority must be grounded in law and in the disputes parties’ consent to arbitrate. As matters stand some treaties are more hospitable to counterclaims than

⁸⁰ See William S. Dodge, *National Courts and International Arbitration: Exhaustion of Remedies and Res Judicata under Chapter 11 of NAFTA*, 23 HASTINGS INT’L & COMP. L. REV. 357, 381–83 (2000).

⁸¹ Douglas, *supra* note 20, at 257.

others. Given the centrality of consent to tribunal authority, the argument that consent can be found in the applicable arbitration rules is tenuous. Explicit reference to counterclaims in the investment treaty itself would eliminate time consuming and inefficient arguments about tribunal authority.

Moving in a direction that favors counterclaims will take some state initiative, and states ought to be thoughtful and careful in how they go about it. If a state wants to ensure that an ISDS tribunal has the authority to hear counterclaims, including an explicit provision in its IIA, along the lines of the one in COMESA 2007,⁸² would obviate the need to make complex arguments about consent and would ensure a tribunal's jurisdictional reach. Treaties should address the privity issues as between the investor and the investment and as between the state and appropriate state entities. Ensuring that the tribunal is directed appropriately towards the applicable law would be helpful, too. Furthermore, limiting the counterclaims to matters based on a concession contract (assuming one is at issue) or that are otherwise closely related to the investment dispute itself would help to allocate authority between the investment tribunal and local courts in a way that reflects their respective areas of expertise.

⁸² Investment Agreement for the COMESA Common Investment Area, *supra* note 21, art. 28(9).