
International Economic Law Clinic

COUNTERCLAIMS IN INTERNATIONAL INVESTMENT LAW

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Abbreviations

BIT	Bilateral Investment Treaty
BLEU	Belgium-Luxembourg Economic Union
COMESA	The Common Market for Eastern and Southern Africa
CPTPP	The Comprehensive and Progressive Agreement for Trans-Pacific Partnership
CSR	Corporate Social Responsibility
ECOWAS	Economic Community of West African States
ECT	Energy Charter Treaty
ICJ	International Court of Justice
ICSID	International Centre for Settlement of Investment Disputes
ICSID Convention	Convention On the Settlement of Investment Disputes Between States and Nationals of Other States
ISDS	Investor-State Dispute Settlement
NAFTA	North American Free Trade Agreement
PAIC	Pan-African Investment Code
OIC	Organization of Islamic Cooperation
SADC	Southern African Development Community
UNCITRAL	The United Nations Commission on International Trade Law
UNCITRAL WG III	The United Nations Commission on International Trade Law Working Group III on Investor-State Dispute Settlement Reform
VCLT	Vienna Convention on the Law of Treaties

Executive Summary

This report engages with the broader conversation on counterclaims in international investment law and the growing trend of including counterclaim provisions within modern investment agreements. It outlines the major issues arising in connection with counterclaims provisions and suggests a model counterclaim provision drawing inspiration from existing treaty practice and the process of reform being carried out at the UNCITRAL Working Group III on Investor-State Dispute Settlement Reform (UNCITRAL WG III).

The **key features of this report** are as follows:

- Analyzing the **procedural requirements** for submission of a state counterclaim under the ICSID Convention, the ICSID Arbitration Rules and the UNCITRAL Arbitration Rules in light of the relevant jurisprudence of arbitral tribunals – particularly **parties’ consent to counterclaims (jurisdiction)** and the existence of a connection **between a state counterclaim and the investor’s primary claim (admissibility) (Section 2)**;
- Identifying the impact of **applicable law provisions** on state counterclaims in light of the relevant jurisprudence of arbitral tribunals **(Section 3.1)**;
- Identifying whether **investor obligations** – when not codified in the investment agreement itself – can be sourced from other provisions in the investment agreement or from contracts related to the investment, the domestic law of the host state, or international law **(Section 3.2)**;
- Critically assessing the **draft counterclaim provision** prepared by **UNCITRAL WG III (i.e. UNCITRAL Draft Provision D)** and identifying its pros and cons **(Section 4)**;
- Engaging in a comparative analysis of **counterclaim provisions** in a selected sample of modern investment agreements and model BITs (see **Figure 1** below) to assess critically alternative wording and the consequences attached to the wording chosen **(Section 5)**;
- Presenting a **model counterclaim provision** based on UNCITRAL Draft Provision D with flexible options for drafting that take into account the practical and theoretical hurdles discussed in the report **(Section 5)**.

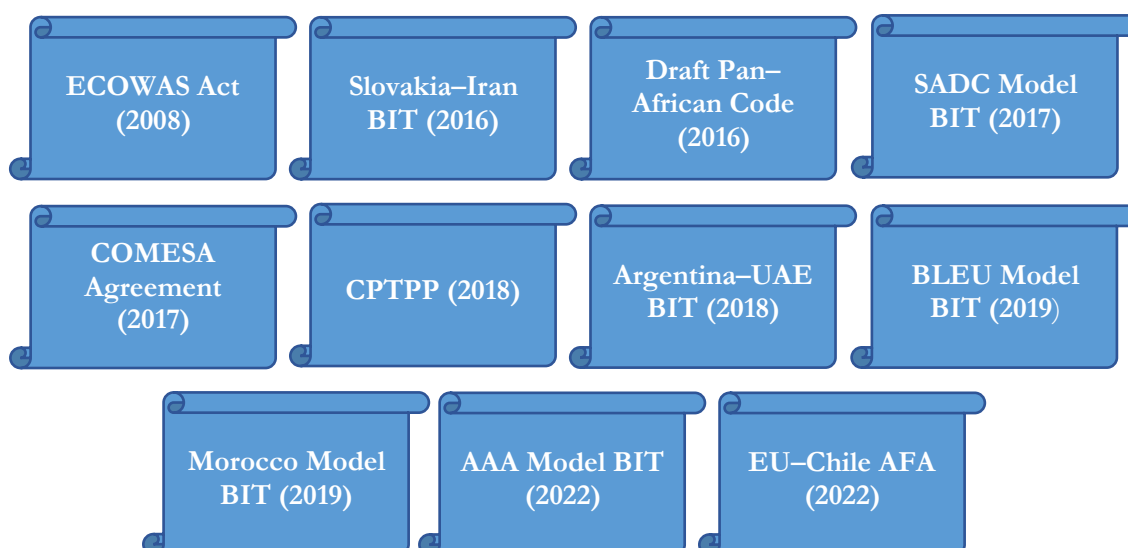


Figure 1: Investment agreements examined in this report

The report answers **two fundamental questions**:

1. How can jurisdiction, admissibility, and applicable law issues arising in connection with counterclaims in ISDS be effectively addressed?
2. What would a model counterclaim provision building on existing treaty practice look like?

Assessing Procedural and Substantive Hurdles for ISDS Counterclaims

This report analyzes how arbitral tribunals have interpreted investment agreements when presented with a state counterclaim and examines whether inconsistencies in their interpretation are owed to differences in treaty language. The key findings, in brief, are as follows:

In relation to **jurisdiction** (*i.e.* **the consent requirement**):

- ICSID and UNCITRAL provide similar requirements regarding consent;
- Consent concerning counterclaims can be implied or express;
- A broad dispute resolution provision, that leaves room for implied consent, makes it more likely that a counterclaim will be heard by an arbitral tribunal;
- Modern investment agreements no longer rely on implied consent and provide for express consent of the parties.

In relation to **admissibility** (*i.e.* **connection requirement**):

- While the ICSID Convention specifically prescribes a connection between a state counterclaim and the investor’s primary claim, the current UNCITRAL Arbitration Rules no longer refer to a connection requirement. However, recent caselaw indicates that – even

under the revised UNCITRAL Arbitration Rules – tribunals investigate whether a connection between a state counterclaim and the investor’s primary claim exists;

- The connection between a state counterclaim and the investor’s primary claim can be either legal or factual. Tribunals’ interpretations of the connection requirement and recent treaty practice addressing this issue are inconsistent. The report finds that it is easier to establish a factual than a legal connection between a counterclaim and the primary claim;
- The caselaw reveals that tribunals enjoy a wide margin of discretion when establishing admissibility. This report finds that tribunals might be willing to move away from a strict legal connection requirement and consider a factual connection as solely sufficient.

In relation to **applicable law**:

- Both Article 42(1) of the ICSID Convention and Article 35(1) of the UNCITRAL Arbitration Rules favor parties’ autonomy and require tribunals to apply the law designated by the parties to the merits of dispute. Parties can choose from a variety of sources, including international law, the domestic law of the host state (or of a third state), or the law of the underlying contract. There is a presumption that this law would also apply to any counterclaims raised by the state against the investor;
- In the absence of an agreement of the parties on the applicable law, Article 42(1) of the ICSID Convention requires tribunals to apply the law of the host state (including its conflict of law rules) and any applicable rules of international law. Article 35(1) of the UNCITRAL Arbitration Rules adopts a more tribunal-centric approach and delegates to the tribunal the determination of the “appropriate” rules to adjudicate the dispute (including any counterclaims).
- While not all investment agreements contain an applicable law provision, states concerned with legal certainty are encouraged to include an applicable law provision in the agreement and to draft it carefully as to include/exclude any sources of law which they want/do not want tribunals to use to adjudicate the dispute, including any counterclaims.

In relation to **investor obligations**:

- The cause-of-action for a counterclaim can either (a) be found in direct investor obligations stipulated in the investment agreement or (b) be sourced indirectly from the law applicable to the merits of the dispute. Old-generation investment agreements tend not to contain any direct investor obligations, but revised and modern investment agreements are

progressively incorporating such obligations, thus strengthening the position of host states willing to submit a counterclaim;

- When direct investor obligations are not expressly codified in the investment agreement, they may be able to be sourced via other provisions in the investment agreement, such as (i) umbrella clauses, or, alternatively, (ii) environmental (and other) exceptions. In practice, however, counterclaims based on investor obligations imported via an umbrella clause or an environmental exception have so far been unsuccessful;
- Similarly, in the absence of direct investor obligations in the investment agreement, these obligations may be able to be sourced indirectly from the underlying contract between the host state and the investor. In practice, however, contract-based counterclaims are also unlikely to succeed if the contract at issue contains (as is often the case) its own forum selection clause. In fact, in these circumstances, arbitral tribunals tend to give effect to such a clause and decline jurisdiction to hear the counterclaim;
- Counterclaims may also be able to be based on obligations of the investor sourced from domestic law. This is, in principle, possible insofar as the investment agreement contains (a) a broad dispute resolution provision and (b) an applicable law provision expressly referring to domestic law. So far, however, counterclaims based on domestic law breaches have been successful only in two exceptional instances, *i.e. Burlington v. Ecuador* and *Perenco v Ecuador*.
- Host states intending to designate domestic law as a source for investor obligations should also consider the consequences of their domestic law being interpreted by international tribunals. Hence, host states concerned about these consequences should explicitly exclude domestic law from the applicable law provision in the investment agreement.
- Finally, counterclaims may also be based on obligations of the investor sourced from international law. As for counterclaims based on domestic law, this is possible, in principle, insofar as the investment agreement contains (a) a broad dispute resolution provision and (b) an applicable law provision expressly referring to international law. While *Urbaser v. Argentina* and *Aven v. Costa Rica* have opened the door for the possibility of investor obligations to be sourced from international law, it should be noted that counterclaims based on international law have so far been unsuccessful.

Model Counterclaim Provision

The report also presents a Model Counterclaim Provision (see **Figure 2** below). While modelled on UNCITRAL Draft Provision D, this Model Provision deviates from the UNCITRAL Draft Provision in certain respects to incorporate select wording from some of the other counterclaim

provisions reviewed in this report (see the Argentina/UAE BIT, the EU/Chile AFA, and the CPTPP).

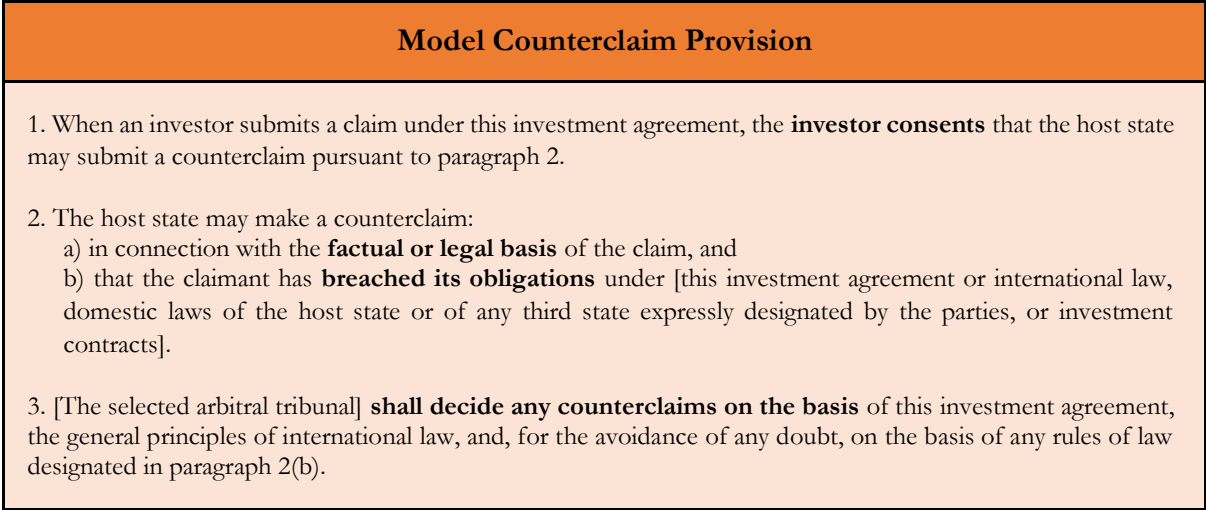


Figure 2: Model Counterclaim Provision (in-depth discussion in **Section 5**)

The report identifies the main issues concerning the language of UNCITRAL Draft Provision D and provides strategic changes to address these issues: (1) it makes the investor’s consent to counterclaims much more explicit; (2) it makes a counterclaim admissible both when a factual or a legal connection between the counterclaim and the investor’s claim exist; and (3) it creates an ad hoc applicable law sub-clause for counterclaims that is distinct from a general applicable law provision. Notably, the suggested counterclaim provision addresses the concerns expressed by some host states that counterclaims may encourage tribunals to interpret their domestic law, thereby interfering with their regulatory autonomy. The wording of the provision is flexible enough to allow room for adjustments by negotiators. **Figure 3** below showcases the most relevant wording drawn upon to create the Model Provision.

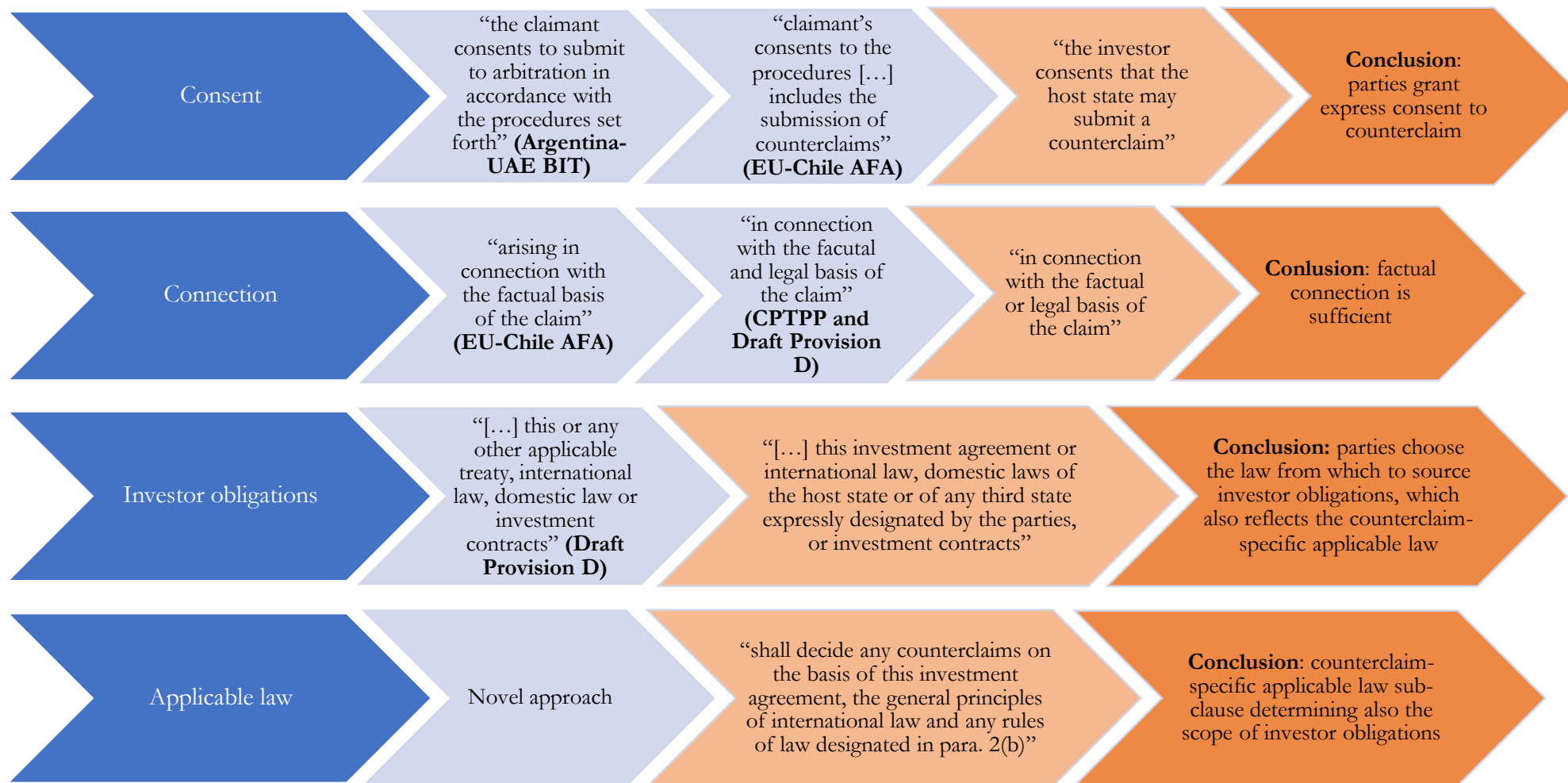


Figure 3: Wording from existing counterclaim provisions that influenced the Model Counterclaim Provision

1 Introduction

The argument that international investment agreements with investor-state dispute settlement (ISDS) have been overly protective of foreign investors at the expense of host states' right to regulate is not novel. Host states have long regarded ISDS one-way system – whereby only investors are entitled to commence proceedings – as asymmetric and have responded to this perceived asymmetry in several ways, including (more recently) by bringing (albeit seldom successfully) counterclaims against foreign investors.

Host states have raised counterclaims on several grounds, including when the investment of a foreign investor causes, either directly or indirectly, environmental and human rights harms. In this sense, counterclaims have also become a powerful tool to address a related concern in international investment law, that is the absence (or rare existence) of investor obligations (*e.g.* to comply with the domestic laws of the host state, to respect human rights, to operate the investment in accordance with environmental standards) in investment agreements. Counterclaims, however, are not a panacea. As the caselaw shows, the practice of arbitral tribunals with respect to counterclaims has not been consistent and counterclaims have frequently generated a significant degree of uncertainty both *vis-à-vis* foreign investors and host states.

This report engages with the broader conversation on counterclaims in international investment law and the growing trend of including counterclaim provisions within modern investment agreements. It outlines the major issues arising in connection with these provisions and suggests a model counterclaim provision drawing inspiration from existing treaty practice and the process of reform being carried out at the UNCITRAL Working Group III on Investor-State Dispute Settlement Reform (UNCITRAL WG III).

This report first identifies the key issues arising in connection with counterclaims, focusing on questions of jurisdiction, admissibility, and applicable law. Second, it engages in a comparative analysis of counterclaim provisions in modern investment agreements and model BITs and proposes a Model Counterclaim Provision using UNCITRAL WG III Draft Provision D as a starting point.

1.1 **Question 1: issues related to jurisdiction, admissibility, and applicable law**

Historically, most counterclaims have been dismissed on jurisdictional and admissibility grounds. More recently, counterclaims have also been dismissed on applicable law grounds. The report

reviews relevant ISDS cases (over twenty) where tribunals ruled on counterclaims with a view to identifying the major challenges to a successful counterclaim (namely, parties’ consent, legal and/or factual connection with the primary claim, and applicable law issues).

The analysis focuses on how arbitral tribunals have interpreted investment agreements when presented with a counterclaim and examines whether inconsistencies in their interpretation are owed to differences in treaty language. These findings, presented in comparative tables, are taken into account in the drafting of the Model Counterclaim Provision presented in the **Section 5** of the report.

1.2 Question 2: a model counterclaim provision inspired by existing treaty practice

Increasingly states have opted to include counterclaim provisions within their modern or revised investment agreements. This report reviews 11 investment agreements and model BITs containing a counterclaim provision (see **Figure 4** below) and engages in a comparative examination of these and other relevant provisions (*e.g.* applicable law provisions, dispute settlement provisions) with a view to identifying potential issues (concerning jurisdiction, admissibility and applicable law) arising in connection with the interpretation of these provisions.

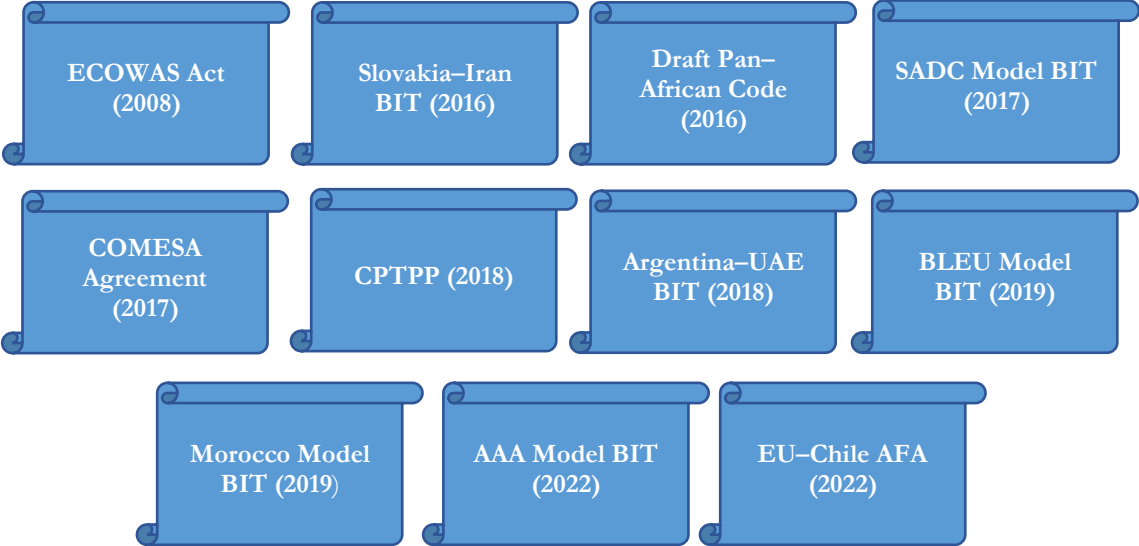


Figure 4: Investment agreements examined in this report

Building on UNCITRAL WG III Draft Provision D, the report also suggests a Model Counterclaim Provision drafted in light of the results of the comparative analysis. While the provision is modelled on Draft Provision D, it deviates from it in certain respects to incorporate select wording from some of the reviewed counterclaim provisions and to address some of the

hurdles to the submission of counterclaims discussed in the report. Notably, the suggested counterclaim provision addresses the concerns expressed by some host states that counterclaims may encourage tribunals to interpret their domestic law, thereby interfering with their regulatory autonomy. The wording of the provision is flexible enough to allow room for adjustments by negotiators.

2 Jurisdiction and Admissibility

ISDS is the main procedural mechanism to settle disputes between host states and foreign investors in international investment law.¹ The International Centre for the Settlement of Investment Disputes (ICSID) and the United Nations Commission on International Trade Law (UNCITRAL) are the main institutions involved in ISDS.² ICSID is a multinational forum for the settlement of investment disputes established under the ICSID Convention and has its own rules of procedure (*i.e.* the ICSID Arbitration Rules). UNCITRAL provides for an alternative framework for ISDS with its own set of arbitration rules (*i.e.* the UNCITRAL Arbitration Rules). This report focuses on these two ISDS frameworks since most cases where arbitral tribunals ruled on counterclaims were ICSID or UNCITRAL cases.

Before an arbitral tribunal can rule on the merits of a claim or a counterclaim, it must first determine whether it has jurisdiction to hear the claim (or the counterclaim), and then establish whether the claim (or the counterclaim) is admissible.³ Jurisdiction is a tribunal's adjudicative power over a claim or a counterclaim; in investment arbitration, such power derives from the parties' consent that their dispute shall be submitted to arbitration.⁴ Admissibility, on the other hand, concerns the appropriateness of a particular claim or counterclaim for adjudication. In other words, while jurisdiction concerns the existence of a tribunal's adjudicative power, admissibility relates to the suitability for a tribunal to exercise such power over a particular claim (or counterclaim).⁵ This categorization, however useful, is not clear-cut and arbitral tribunals have added to the confusion surrounding the boundary between jurisdiction and admissibility by interpreting these concepts rather flexibly and to some extent inconsistently.⁶ Notwithstanding this inconsistency, this report discusses both concepts separately in an attempt to outline the different issues arising in connection with jurisdictional and admissibility objections to counterclaims as evidenced in the relevant (and scattered) caselaw.⁷

¹ Rudolf Dolzer, Ursula Kriebaum and Christoph Schreuer, *Principles of International Investment Law* (Oxford University Press 2022), p. 13.

² *Id.* at p. 11.

³ Tomoko Ishikawa, *Corporate Environmental Responsibility in Investor-State Dispute Settlement, The Unexhausted Potential of Current Mechanisms* (Cambridge University Press 2022), p. 88 referring to *Aven v. Costa Rica*: "counterclaims must meet the requirements of jurisdiction and admissibility 'in the same way the main claim does' in order to be admitted". See *David R. Aven and Others v. Republic of Costa Rica (Aven v. Costa Rica)*, ICSID Case No. UNCT/15/3, Award (18 September 2018), para. 745.

⁴ Laurent Gouiffès and Melissa Ordonez, 'Jurisdiction and Admissibility: Are We Any Closer to a Line in the Sand?' (2015) 31(1) *Arbitration International*, pp. 108-10.

⁵ *Ibid.*

⁶ *Id.* at pp. 110-11.

⁷ *Id.* at pp. 108-10.

2.1 Counterclaims under the ICSID Convention and the ICSID Arbitration Rules

A counterclaim is an autonomous claim brought by the host state seeking a remedy based on grounds distinct, but closely related to, those of the primary claim.⁸ In this sense, it differs from a pleading to set-off. The ICSID Convention, supplemented by the ICSID Arbitration Rules, expressly allows states to bring counterclaims against a foreign investor, provided they meet the requirements of Article 46 of the ICSID Convention and Rule 48 of the ICSID Arbitration Rules⁹ (see **Figure 5** below).¹⁰

Article 46 ICSID Convention
<u>Powers and Functions of the Tribunal</u>
<p>Except as the parties otherwise agree, the Tribunal shall, if requested by a party, determine any incidental or additional claims or counterclaims 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.</p>
Rule 48 ICSID Arbitration Rules
<u>Ancillary Claims</u>
<p>(1) Unless the parties agree otherwise, a party may file an incidental or additional claim or a counterclaim (“ancillary claim”) arising directly out of the subject-matter of the dispute, provided that such ancillary claim is within the scope of the consent of the parties and the jurisdiction of the Centre.</p> <p>(2) An incidental or additional claim shall be presented no later than in the reply, and a counterclaim shall be presented no later than in the counter-memorial, unless the Tribunal decides otherwise.</p> <p>(3) The Tribunal shall fix time limits for submissions on the ancillary claim.</p>

Figure 5: Article 46 of the ICSID Convention and Rule 48 of the ICSID Arbitration Rules

⁸ Ishikawa (n 3), p. 58.

⁹ As amended effective 1 July 2022. Rule 48 ICSID Arbitration Rules was former Rule 40, which provided: “(1) Except as the parties otherwise agree, a party may present an incidental or additional claim or counter-claim arising directly out of the subject-matter of the dispute, provided that such ancillary claim is within the scope of the consent of the parties and is otherwise within the jurisdiction of the Centre. (2) An incidental or additional claim shall be presented not later than in the reply and a counter-claim no later than in the counter- memorial, unless the Tribunal, upon justification by the party presenting the ancillary claim and upon considering any objection of the other party, authorizes the presentation of the claim at a later stage in the proceeding”; available at <<https://icsid.worldbank.org/sites/default/files/ICSID%20Convention%20English.pdf>> accessed 10 December 2022.

¹⁰ Melissa Ordonez, ‘States’ Counterclaims: How Hard Is It to Counterattack in International Investment Arbitration?’ (2019) 22(1) International Arbitration Law Review, p. 29; Arnaud de Nanteuil, ‘Counterclaims in Investment Arbitration: Old Questions, New Answers’ (2018) 17(2) The Law & Practice of International Courts and Tribunals, p. 375.

In particular, the requirements that must be satisfied for a counterclaim to be heard at the merits stage are as follows:¹¹

1. the counterclaim must be “within the consent of the parties” (*i.e.* **consent requirement**);
2. the counterclaim must “arise directly out of the subject-matter of the dispute” (*i.e.* **connection requirement**);
3. the parties must have not agreed otherwise;
4. the counterclaim must be requested by a party;
5. the counterclaim must be “otherwise within the jurisdiction of the Centre”.¹²

The analysis below focuses exclusively on (1) the **consent requirement** (*i.e.* **jurisdiction**) and (2) the **connection requirement** (*i.e.* **admissibility**) as these have been the primary impediments to most counterclaims in ISDS.

2.1.1 Consent Requirement

Consent is a crucial part of the jurisdiction test and one of the main reasons why tribunals have denied jurisdiction over state counterclaims in the past.¹³ Consent is an “agreement of parties to the same thing”, or, more simply, a “meeting of the minds”.¹⁴

Host states express their consent to arbitrate by entering into – and hence becoming parties to – investment agreements. Investors, on the other hand, are not per se parties to investment agreements; they express their consent to arbitrate by accepting the host state’s unilateral offer to arbitrate when they file a claim against the host state under the terms of the agreement. Consent to counterclaims can be expressly provided in the dispute resolution provision or it can be implied from the terms of the investment agreement.¹⁵ Such determination is made pursuant to the rules

¹¹ Stephan W. Schill, *Schreuer’s Commentary on the ICSID Convention: A Commentary on the Convention on the Settlement of Investment Disputes between States and Nationals of Other States* (Oxford University Press 2022), pp. 1029-36.

¹² Article 25(1) of the ICSID Convention provides for the following additional requirements: (1) the counterclaim must relate to a legal dispute arising directly out of an investment covered by the ICSID Convention (*see e.g. Amco v. Indonesia* where the tribunal considered that, since the counterclaim was not directly based on an investment within the meaning of Article 25(1), it did not fall within its jurisdiction (*Amco Asia Corporation and others v. Republic of Indonesia (Amco v. Indonesia)*, ICSID Case No. ARB/81/1, Decision on Jurisdiction in Resubmitted Proceeding (10 May 1998), paras. 122, 125)); (2) the counterclaim must relate to a legal dispute between a host state and an investor (*i.e.* the disputing parties) as defined by the ICSID Convention; and (3) the counterclaim must fall within the written consent of the disputing parties, which cannot be withdrawn unilaterally.

¹³ Anne K. Hoffmann, ‘Chapter 36: Counterclaims’, in Meg Kinnear et al. (eds), *Building International Investment Law: The First 50 Years of ICSID*, (Kluwer 2015), pp. 519-20; Carlo de Stefano, ‘Equality and Asymmetry in Treaty-Based Investment Arbitration: Counterclaims by Host States’ in Daniele Amoroso et al. (eds), *More Equal than Others? Perspectives on the Principle of Equality from International and EU Law* (Springer 2023), p. 310.

¹⁴ Black’s Law Dictionary (11th edn. 2019).

¹⁵ Consent to counterclaims can also be established from a contract between the host state and the investor, or from the host state’s national legislation, or again from a separate arbitration agreement. In *Burlington v. Ecuador*, for example,

of interpretation set out in the Vienna Convention on the Law of Treaties (VCLT), and in particular in Article 31 of the VCLT.¹⁶

When determining consent to state counterclaims, arbitral tribunals primarily consider the wording of the dispute resolution provision and examine (a) whether the host state has a right to bring a counterclaim against the investor and (b) whether disputes based on obligations of the investor are covered under the investment agreement.¹⁷ An overview of the caselaw shows that dispute resolution provisions can be categorized into two types of provisions: (1) narrow dispute resolution provisions, exclusively covering disputes concerning obligations of the host state, and (2) broad dispute resolution provisions, which do not limit the scope of the parties' consent to disputes concerning obligations of the host state.¹⁸ **Figure 6** below provides examples of both types of dispute settlement provision.¹⁹

(1) Narrow Dispute Resolution Provision
For example: <ul style="list-style-type: none">▪ "... disputes ... concerning an obligation of the latter [host State]"²⁰ (Art. 9 Greece/Romania BIT)▪ "... disputes ... relating to a claim by the investor that a measure taken or not taken by [the host State] is in breach of this Agreement" (Art. XII Canada/Venezuela BIT)
(2) Broad Dispute Resolution Provision
For example: <ul style="list-style-type: none">▪ "... a dispute relating to an investment" (Art. 8(1) BLEU/Burundi BIT)▪ "Disputes ... concerning investments within the meaning of this Agreement" (Art. X Argentina/Spain BIT)

Figure 6: Examples of narrow and broad dispute resolution provisions

Burlington and Ecuador entered into a separate agreement on 26 May 2011 – notably, two years after the primary claim was filed with the tribunal – in which they expressed their consent that the arbitral tribunal was the “appropriate forum for the final resolution of the Counterclaims arising out of the investments made by Burlington Resources [...]” See *Burlington Resources Inc. v. Republic of Ecuador (Burlington v. Ecuador)*, ICSID Case No. ARB/08/5, Decision on Counterclaims (7 February 2017), para. 60. See also Dolzer, Kriebaum and Schreuer (n 1), p. 360.

¹⁶ See e.g. *Spyridon Roussalis v. Romania (Roussalis v. Romania)*, ICSID Case No. ARB/06/1, Award (7 December 2011), para. 869.

¹⁷ Hege E. Kjos, *Applicable Law in Investor-State Arbitration: The Interplay Between National and International Law* (Oxford University Press 2013), p. 133.

¹⁸ De Nanteuil (n 10), p. 378.

¹⁹ *Ibid.*

²⁰ See also Article 8 UK/Venezuela BIT.

The wording of **narrow dispute resolution provisions** has often been considered decisive in reaching a conclusion that the tribunal did not have jurisdiction to hear a state counterclaim. **Figure 7** below provides three examples of cases where an arbitral tribunal (or, as in *Roussalis v. Romania*, the majority of the tribunal) denied jurisdiction on the grounds that the narrow dispute resolution provision in question precluded state counterclaims.

Caselaw	Relevant Provision	Analysis of the Tribunal
<p><i>Spyridon Roussalis v. Romania</i>, ICSID Case No. ARB/06/1, Award dated 7 December 2011</p>	<p>Article 9 Greece–Romania BIT</p> <p>(1) Disputes between an investor of a Contracting Party and the other Contracting Party concerning an obligation of the latter under this Agreement, in relation to an investment of the former, [...]</p>	<p>The wording “disputes [...] concerning an obligation of the latter’ undoubtedly limit[s] jurisdiction to claims brought by investors about obligations of the host State. Accordingly, the BIT does not provide for counterclaims to be introduced by the host state in relation to obligations of the investor.” (para. 869)</p>
<p><i>Vestey Group v. Bolivarian Republic of Venezuela</i>, ICSID Case No. ARB/06/4, Award dated 15 April 2016</p>	<p>Article 8 UK–Venezuela BIT</p> <p>(1) Disputes between a national or company of one Contracting Party and the other Contracting Party concerning an obligation of the latter under this Agreement in relation to an investment of the former [...]</p>	<p>The scope of the consent is limited to “[d]isputes between a national or company of one Contracting Party and the other Contracting Party concerning an obligation of the latter under this Agreement in relation to an investment of the former [...]” (para. 333)</p>
<p><i>Rusoro Mining Ltd. v. Bolivarian Republic of Venezuela</i>, ICSID Case No. ARB(AF)/12/5, Award dated 22 August 2016</p>	<p>Article XII Canada–Venezuela BIT</p> <p>(1) Any dispute [...] relating to a claim by the investor that a measure taken or not taken by the former Contracting Party is in breach of this Agreement, [...]</p> <p>(3) An investor may submit [...]:</p> <p>(a) the investor has consented in writing thereto; [...]</p>	<p>The “literal wording of Art. XII does not leave room for doubt: the Treaty affords investors, and only investors, standing to file arbitrations against host States.” Therefore, the tribunal “finds that it lacks jurisdiction to adjudicate the counter-claim submitted by the Bolivarian Republic against Rusoro.” (paras. 627, 629)</p>

Figure 7: Relevant cases where tribunals interpreted narrow dispute settlement provisions as not granting them jurisdiction over state counterclaims

Relevantly, in *Roussalis v. Romania*, Reisman (in dissent) argued that consent to counterclaims can be derived from the reference to the ICSID Convention in the treaty’s dispute resolution provision. In his words:

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.²¹

This approach would serve both the host state and the investor as it would ensure procedural efficiency and dispense the investor from becoming involved in parallel proceedings before a domestic court, the very “forum” which the investor “avoided when filing its principal claims”.²²

Notably, in *Gavazzi v. Romania*, the majority of the arbitral tribunal interpreted narrowly a broad dispute resolution provision (see **Figure 8** below).²³ On closer scrutiny, however, only paragraph 1 of Article 8 of the Italy/Romania BIT is drafted broadly, as paragraph 2 narrows down the scope of the provision by stating that it is “the investor” that may submit a dispute to arbitration. Paragraph 2 has been interpreted by the arbitral tribunal as “only grant[ing] the investor the right to claim against the Host State”.²⁴

Caselaw	Relevant Provision	Analysis of the Tribunal
<p><i>Marco Gavazzi and Stefano Gavazzi v. Romania</i>, ICSID Case No. ARB/12/25, Decision on Jurisdiction, Admissibility and Liability dated 21 April 2015</p>	<p>Article 8 Italy–Romania BIT²⁵</p> <p>(1) Any dispute between one Contracting Party and an investor of the other Contracting Party concerning an investment of that investor in the territory of the former Contracting Party [...]</p> <p>(2) In the event that the dispute cannot be resolved amicably within six months of the date of a written request, the investor in question may submit the dispute at his discretion [...]</p>	<p>The tribunal considered “that it is the letter of the BIT, interpreted under international law, that binds the Parties”. “[T]he language of Article 8 “may seem to indicate that also the claims of the Host State [...] should be covered by the BIT. However, [...] Article 8(2) of the BIT only grants the investor the right to claim against the Host State.” (paras. 151, 154)</p> <p>Further, the majority considered that “where there is no jurisdiction provided by the wording of the BIT in relation to a counterclaim, no jurisdiction can be inferred merely from the ‘spirit’ of the BIT.” (para. 154)</p>

Figure 8: *Gavazzi v. Romania*

²¹ *Spyridon Roussalis v. Romania (Roussalis v. Romania)*, ICSID Case No. ARB/06/1, Declaration (Dissenting Opinion of Reisman) (28 November 2011).

²² Ishikawa (n 3), p. 93, who argues that the tribunal in *Goetz v Burundi (II)* adopted the same “importing consent” approach. See *Antoine Goetz & Consorts et S.A. Affinage des Métaux v. Republic of Burundi (Goetz v. Burundi (II))*, ICSID Case No. ARB/01/2, Award (21 June 2012), paras. 279-80

²³ *Marco Gavazzi and Stefano Gavazzi v. Romania (Gavazzi v. Romania)*, ICSID Case No. ARB/12/25, Decision on Jurisdiction, Admissibility and Liability (21 April 2015), paras. 151-54.

²⁴ *Id.* at para. 151.

²⁵ Original text in Italian: “Articolo 8(2): Nel caso in cui tale controversia non possa essere risolta amichevolmente entro sei mesi dalla data di una richiesta scritta, l’investitore in questione potrà sottoporre la controversia -a sua discrezione [...]”. English translation available at <https://edit.wti.org/document/show/78a08726-e8fd-4de6-9976-59e357745191> accessed 10 December 2022.

Rubino-Sammartano (in dissent) interpreted this provision as not precluding state counterclaims. He stated:

[...] The omission of any express mention of the Host State’s right to file a counterclaim may be due to the fact that the drafters of the BIT focused on the protection of the investor. One has then to consider whether this omission excludes any counterclaim by the Host State against the investor before the arbitration forum provided by the BIT. Art. 46 of the ICSID Convention and Rule 40 of its Arbitration Rules provide for counterclaims. The Respondent’s counterclaim is for damages caused by the investor, which arise from the investment – or more precisely the failure of investments – and thus allegedly from the same subject matter of the Parties’ dispute. [...] **It would be hard to accept that the BIT’s Contracting Parties intended to give rise to parallel proceedings before different courts and tribunals**, by preventing the Host State from asserting its rights against the investor in a counterclaim. In my opinion, in the present proceedings, a free-standing counterclaim is admissible on the above grounds, **due process includes the right to defend a claim** and in my opinion **natural justice requires that such defence may include making a counterclaim related to such issues.**²⁶

Gavazzi, however, is an outlier. In most cases where the **dispute resolution provision** in question was drafted **broadly**, tribunals upheld jurisdiction to hear a state counterclaim (e.g. in *Urbaser v. Argentina*, see **Figure 9** below).

Caselaw	Relevant Provision	Analysis of the Tribunal
<p><i>Urbaser S.A. and Consorcio de Aguas Bilbao Bizkaia, Bilbao Biskaia Ur Partzuergoa v. The Argentine Republic</i>, ICSID Case No. ARB/07/26, Award dated 8 December 2016</p>	<p>Article X Argentina–Spain BIT²⁷</p> <p>(1) Disputes arising between one of the Parties and an investor of the other Party concerning investments within the meaning of this Agreement [...]</p> <p>(3) The dispute may be submitted to an international arbitral tribunal in any of the following circumstances:</p> <p>(a) at the request of one of the parties to the dispute, [...]</p> <p>(b) Where both parties to the dispute have so agreed.</p>	<p>Article X(1) “is completely neutral as to the identity of the claimant or respondent in an investment dispute arising between the parties.” Article X (3) clearly provides “that either the investor or the host State can be a party submitting a dispute in connection with an investment to arbitration.” (para. 1143)</p>

Figure 9: *Urbaser v. Argentina*

²⁶ *Gavazzi v. Romania*, Dissenting Opinion of Mauro Rubino- Sammartano (21 April 2015), para. 42(i) (emphasis added).
²⁷ Original text in Spanish: “(1) Las controversias que surgieren entre una de las Partes y un inversor de la otra Parte en relación con las inversiones en el sentido del presente Acuerdo, deberán, en lo posible, ser amigablemente dirimidas entre las partes en la controversia. [...] (3) La controversia podrá ser sometida a un tribunal arbitral internacional en cualquiera de las circunstancias siguientes: a. A petición de una de las partes en la controversia, [...] b. Cuando ambas partes en la controversia así lo hayan convenido.” English translation available at <https://edit.wti.org/app.php/document/show/906eff11-67f0-4fed-afb9-3f6a725b5c76> accessed 10 December 2022.

2.1.2 Connection Requirement

Admissibility is the second challenge to the success of a state counterclaim. This concerns the connection between the primary claim and the counterclaim. Article 46 of the ICSID Convention and Rule 48(1) of the ICSID Arbitration Rules provide that a counterclaim, in order to be admissible, must arise “directly out of the subject-matter of the dispute”. In other words, a counterclaim is admissible when it is connected to the primary claim.

The connection between the primary claim and the counterclaim can be either legal or factual.²⁸ To establish a legal connection, the primary claim and the counterclaim must be based on the same legal instrument (*e.g.* the same investment agreement or the same contract).²⁹ A factual connection, on the other hand, looks at whether the counterclaim relates to the same facts as the ones giving rise to the primary claim.³⁰ The ICSID Secretariat explained that a factual connection can be established when such “factual connection between the original and the ancillary claim is so close as to require the adjudication of the latter in order to achieve the final settlement of the dispute, the object being to dispose of all the grounds of dispute arising out of the same subject matter”.³¹

In practice, distinguishing between a legal and a factual connection is not straightforward; tribunals have been inconsistent and opted for a determination that either one or the other existed without satisfactorily elaborating on their reasoning.³²

In *Gavażzi*, for example, the majority of the tribunal dismissed a state counterclaim on admissibility grounds due to the inexistence of a legal connection between the primary claim and the counterclaim (*see* **Figure 10** below).³³

²⁸ *Urbaser S.A and Consorcio de Aguas Bilbao Bizkaia, Bilbao Biskaia Ur Partzuergoa v. The Argentine Republic (Urbaser v. Argentina)*, ICSID Case No. ARB/07/26, Award (8 December 2016), para. 1151.

²⁹ De Nanteuil (n 10), p. 388.

³⁰ *Id.* at pp. 386-87.

³¹ ICSID Regulations and Rules (International Center for Settlement of Investment Disputes, 1 January 1968), Note B(a) to Arbitration Rule 40, pp. 105-6.

³² Ordonez (n 10), p. 32.

³³ A similar approach was followed in *Saluka Investments B.V. v. The Czech Republic (Saluka v. Czech Republic)*, UNCITRAL Decision on Jurisdiction over the Czech Republic’s Counterclaim (7 May 2004), para. 79 and *Sergei Pausbok, CJSC Golden East Company and CJSC Vostokneftegaz Company v. The Government of Mongolia (Pausbok v. Mongolia)*, UNCITRAL, Award on Jurisdiction and Liability (29 April 2011), para. 694 – both, however, UNCITRAL cases.

Caselaw	Analysis of the Tribunal
<p><i>Marco Gavazzi and Stefano Gavazzi v. Romania</i>, ICSID Case No. ARB/12/25, Decision on Jurisdiction, Admissibility and Liability dated 21 April 2015</p>	<p>“The majority further observes that the counterclaim submitted by the Respondent is an entirely independent claim based upon Romanian law and unrelated to the Claimant’s claim based upon breaches of the BIT. Both in form and substance, it is a free-standing counterclaim not operating merely as a defense to the Claimant’s claim.” (para. 154)</p>

Figure 10: *Gavazzi v. Romania*: an example of a case where the legal connection requirement was not met

Relevantly, Rubino-Sammartano (in dissent) disagreed with the majority of the tribunal, including on their finding on admissibility. He argued that the counterclaim should be admissible because:

[t]he Respondent’s counterclaim is for damages caused by the investor, which **arise from the investment** - or more precisely the failure of investments - and thus allegedly from the **same subject matter as the Parties’ dispute**.³⁴

This case shows that tribunals are reluctant to admit a state’s counterclaim when they consider that the counterclaim is not sufficiently connected to the primary claim, for example because the counterclaim is based on an breach of domestic law or an obligation arising from the underlying contract, while the primary claim is based on an breach of the investment agreement.³⁵ This strict application of the legal connection requirement has been criticized for limiting the ability of host states to bring counterclaims.³⁶

The factual connection requirement, conversely, is more easily met. **Figure 11** below shows several examples of cases where a state counterclaim was considered admissible on the grounds that there was a sufficiently strong factual connection between the counterclaim and the primary claim.

³⁴ *Gavazzi v. Romania*, Dissenting Opinion of Rubino-Sammartano, (n 26), para. 42(i).

³⁵ Ted Gleason, ‘Examining Host State Counterclaims for Environmental Damage in Investor State Dispute Settlement From Human Rights and Transnational Public Policy Perspectives’ (2021) 21(3) International Environmental Agreements: Politics, Law and Economics, p. 430.

³⁶ See Xuan Shao, ‘Environmental and Human Rights Counterclaims in International Investment Arbitration: At The Crossroads of Domestic and International Law’ (2021) 24(1) Journal of international Economic Law, p. 169; Zachary Douglas, *The international Law of Investment Claims*, (Cambridge University Press 2009), pp. 260-63; Hege E. Kjos, ‘Counterclaims by Host States in Investment Treaty Arbitration’ (2007) 4 Transnational Dispute Management, pp. 43-46; De Stefano (n 13), p. 323.

Caselaw	Analysis of the Tribunal
<p><i>Antoine Goetz & Consorts et S.A. Affinage des Métaux v Republic of Burundi (II)</i>, ICSID Case No. ARB/01/2, Award dated 21 June 2012</p>	<p>The tribunal concluded that the counterclaim was arising out of the same subject-matter of the primary dispute because the damage alleged by Burundi was a result of the same breaches established in the primary claim. (para. 285)³⁷</p>
<p><i>Urbaser S.A. and Consorcio de Aguas Bilbao Bizkaia, Bilbao Biskaia Ur Partzuergoa v. The Argentine Republic</i>, ICSID Case No. ARB/07/26, Award dated 8 December 2016</p>	<p>The tribunal observes that “the factual link between the two claims is manifest. Both the principal claim and the claim opposed to it are based on the same investment, or the alleged lack of sufficient investment, in relation to the same Concession. This would be sufficient to adopt jurisdiction over the counterclaim as well. The legal connection is also established to the extent the Counterclaim is not alleged as a matter based on domestic law only.” (para. 1151)</p>
<p><i>Burlington Resources Inc. v. Republic of Ecuador</i>, ICSID Case No. ARB/08/5, Decisions on Ecuador’s Counterclaims dated 7 February 2017</p>	<p>When analyzing the conditions of Article 46 of the ICSID Convention, the tribunal stated that: “these conditions are met here: (i) the counterclaims arise directly out of the subject-matter of the dispute, namely Burlington’s investment in Blocks 7 and 21; [...]” (para. 62)</p>

Figure 11: Relevant cases where the factual connection requirement was met

The caselaw examined above shows that tribunals enjoy a wide margin of discretion under the ICSID rules and that they may be willing to move away from the strict legal connection requirement and consider a factual connection as solely sufficient.³⁸

2.2 Counterclaims under the UNCITRAL Arbitration Rules

Under the UNCITRAL Arbitration Rules, counterclaims are expressly allowed, provided they meet the requirements of Article 21(3), formerly Article 19(3) (*see Figure 12* below).³⁹

³⁷ Original text in French: “Le différend principal relatif à ABC concernait la licéité de la suspension du certificat d’entreprise de zone franche et la fermeture consécutive de la banque à la suite de manquements à ses obligations. La demande reconventionnelle concerne le préjudice allégué par le Burundi du fait de ces mêmes manquements. Elle est donc en rapport direct avec l’objet du différend et est par suite recevable.”

³⁸ Shao (n 36), p. 168.

³⁹ The UNCITRAL Arbitration Rules were revised in 2010 (Article 19(3) was replaced by Article 21(3)) and again in 2013; the wording of Article 21(3), however, has remained the same.

UNCITRAL Arbitration Rules (1976 version)	UNCITRAL Arbitration Rules (2010 and 2013 version)
<p>Article 19(3)</p> <p>In his statement of defence, or at a later stage in the arbitral proceedings if the arbitral tribunal decides that the delay was justified under the circumstances, the respondent may make a counterclaim arising out of the same contract or rely on a claim arising out of the same contract for the purpose of a set-off.</p>	<p>Article 21(3)</p> <p>In its statement of defence, or at a later stage in the arbitral proceedings if the arbitral tribunal decides that the delay was justified under the circumstances, the respondent may make a counterclaim or rely on a claim for the purpose of a set-off provided that the arbitral tribunal has jurisdiction over it.</p>

Figure 12: 1976, 2010 and 2013 UNCITRAL Arbitration Rules

Article 21(3) of the UNCITRAL Arbitration Rules stipulates that counterclaims may be considered by an arbitral tribunal provided that they meet two main conditions:

1. the counterclaim must be raised by the respondent in its statement of defence;⁴⁰ and
2. the counterclaim must be within the jurisdiction of the tribunal.

ICSID and UNCITRAL tribunals have faced similar legal questions when determining whether the consent and connection requirements are met. This report has already examined these issues in **Section 2.1** above. **Sections 2.2.1** and **2.2.2** highlight the differences (if any) emerged in relation to the application of the UNCITRAL Arbitration Rules.

2.2.1 Consent Requirement

Unlike the ICSID Convention and the ICSID Arbitration Rules, the UNCITRAL Arbitration Rules do not offer any guidance as to how a tribunal can establish that it has jurisdiction to hear a counterclaim.⁴¹ Irrespective of this, it is commonly understood that consent is implicitly required under Article 21(3). Hence, building on ICSID tribunals' practice, UNCITRAL tribunals commonly look for evidence of the parties' consent to counterclaims.⁴² In particular, UNCITRAL tribunals typically examine whether the dispute resolution provision in the relevant investment agreement is narrowly worded, or, rather, broad enough to encompass counterclaims.⁴³

⁴⁰ A counterclaim may be submitted at a later stage but, if so, the respondent must provide an explanation for the delay. As per Article 21(3), the tribunal exercises discretion on whether to accept the respondent's reasons for the delay. The tribunal may consider due process concerns such as a "possible prejudice caused to the claimant by the acceptance of the late submission of the counterclaim, and the effect of the delay on the arbitral proceedings as a whole". In practice, counterclaims that are submitted late are rarely admitted. David D. Caron and Lee M. Caplan, *The UNCITRAL Arbitration Rules - A Commentary* (Oxford University Press 2013), pp. 425-26.

⁴¹ Clyde Croft, Christopher Kee and Jeff Waincymer, *A Guide to the UNCITRAL Arbitration Rules* (Cambridge University Press 2013), para. 21.15.

⁴² Kjos, *Applicable Law* (n 17), p. 130.

⁴³ De Nanteuil (n 10), pp. 376-78.

In *Saluka v. Czech Republic*, for example, an UNCITRAL tribunal found that it had jurisdiction to hear state counterclaims on the grounds that the relevant dispute resolution clause was sufficiently broad. A similar conclusion was reached in *Aven v. Costa Rica* (see **Figure 13** below).

Caselaw	Relevant Provision	Analysis of the Tribunal
<p><i>Saluka Investments B.V. v. The Czech Republic</i>, UNCITRAL Decision on Jurisdiction over the Czech Republic’s Counterclaim dated 7 May 2004</p>	<p>Article 8 Czech Republic–Netherlands BIT</p> <p>(1) All disputes between one Contracting Party and an investor of the other Contracting Party concerning an investment of the latter [...]</p> <p>(2) Each Contracting Party consents to submit a dispute referred to in paragraph (1) of this Article, to an arbitral tribunal, [...]</p>	<p>The tribunal considered that the dispute resolution provision is broad enough to include counterclaims. Further, both parties accepted that counterclaims might fall within the scope of the tribunal’s jurisdiction and the parties’ consent. (paras. 37-39)</p>
<p><i>David R. Aven and Others v. Republic of Costa Rica</i>, ICSID Case No. UNCT/15/3, Award dated 18 September 2018</p>	<p>Article 10.15 DR-CAFTA</p> <p>In the event of an investment dispute, the claimant and the respondent should initially seek to resolve through consultation and negotiation [...]</p> <p>Article 10.16 DR-CAFTA</p> <p>(1) In the event that a disputing party considers that an investment dispute cannot be settled by consultation and negotiation:</p> <p>(a) the claimant, on its own behalf, may submit to arbitration under this Section a claim [...]</p>	<p>The tribunal considered that “the language of Articles 10.15 and 10.16 of DR-CAFTA is in principle wide enough to encompass counterclaims and [...] Article 10.16 does not imply that it applies only to disputes in which it is an investor which initiates claims.” (para. 740)</p> <p>The tribunal also referred to Reisman’s statement (in dissent) in <i>Roussalis v. Romania</i> and held that allowing counterclaims has “several practical advantages in terms of procedural economy and efficiency.” (paras. 731-42)</p>

Figure 13: Cases where tribunals found that the relevant dispute resolution provision was sufficiently broad to encompass counterclaims

Conversely, in *Oxus v. Uzbekistan*, an UNCITRAL tribunal, following ICSID tribunals’ practice, denied jurisdiction to hear the host state’s counterclaims on the grounds that the relevant dispute resolution provision was narrowly worded (see **Figure 14** below). Building on the reasoning in *Saluka*, the tribunal further considered whether there was a close connection between the investor’s claims and the counterclaims which could have exceptionally allowed it to hear the counterclaim. In the end the tribunal found that it had not jurisdiction to hear the host state’s counterclaims.⁴⁴

⁴⁴ *Oxus Gold v. Republic of Uzbekistan (Oxus v. Uzbekistan)*, UNCITRAL, Final Award (17 December 2015), paras. 948-59.

Caselaw	Relevant Provision	Analysis of the Tribunal
<p><i>Oxus Gold v. Republic of Uzbekistan</i>, UNCITRAL, Final Award dated 17 December 2015</p>	<p>Article 8 UK–Uzbekistan BIT</p> <p>(1) Disputes between a national or company of one Contracting Party and the other Contracting Party concerning an obligation of the latter under this Agreement [...]</p>	<p>The tribunal found that the wording in Article 8 indicates “that the Parties’ consent to arbitration under the BIT only covers claims from investors against the host State, but not claims from the host State against the investors, to the possible exception of counter-claims having a close connection with the investor’s claims.” (para. 948)</p>

Figure 14: *Oxus v. Uzbekistan*

In addition to the question of whether a dispute resolution provision is drafted narrowly or broadly as to cover counterclaims, a few arbitral tribunals, when determining consent, have also considered whether the relevant investment agreement *prima facie* includes investor obligations.⁴⁵ In *Al-Warrag v. Indonesia*, for example, an UNCITRAL tribunal used the investor obligation stipulated in the investment agreement as an interpretive tool to confirm its finding that the dispute resolution clause (admittedly broadly worded) “permit[ted] counterclaims by the respondent state”.⁴⁶

2.2.2 Connection Requirement

The 1976 version of the UNCITRAL Arbitration Rules expressly required that a counterclaim, to be admissible, “aris[e] out of the same contract” as the primary claim. This express requirement, stipulated at Article 19(3), was removed in the 2010 revision of the rules.⁴⁷ Hence, in principle, under the new Article 21(3), counterclaims may also be admissible when arising from separate but related agreements between the parties.⁴⁸ In practice, however, even under the new Article 21(3), tribunals still look for the existence of a sufficient connection between the primary claim and the counterclaim when determining whether a counterclaim is admissible.⁴⁹

⁴⁵ Scholars have been critical of the view that the jurisdiction of a tribunal to hear a counterclaim should only depend on the dispute resolution provision. See Ordonez (n 10), p. 31; Shahrizal M. Zin, ‘Chapter 11: Reappraising Access to Justice in ISDS: A Critical Review on State Recourse to Counterclaim’, in Alan M. Anderson and Ben Beaumont (eds), *The Investor-State Dispute Settlement System: Reform, Replace or Status Quo?* (Kluwer Law International 2020), p. 234; De Nanteuil (n 10), p. 382.

⁴⁶ Hesham T.M. *Al Warrag v. Republic of Indonesia (Al Warrag v. Indonesia)*, UNCITRAL, Final Award (15 December 2014), paras. 662-63. The tribunal based its interpretation on Article 9 of the OIC Agreement (“The investor shall be bound by the laws and regulations in force in the host state and shall refrain from all acts that may disturb public order or morals or that may be prejudicial to the public interest. He is also to refrain from exercising restrictive practices and from trying to achieve gains through unlawful means.”) and Article 17(2)(a) of the OIC Agreement (“[...] then each party has the right to resort to the Arbitration Tribunal for a final decision on the dispute”).

⁴⁷ See Dafina Atanasova, Adrián Martínez Benoit, Josef Ostranský, ‘The Legal Framework for Counterclaims in Investment Treaty Arbitration’ (2014) 31(3) *Journal of International Arbitration*, p. 364.

⁴⁸ Thomas Kendra, ‘State Counterclaims in Investment Arbitration - A New Lease of Life?’ (2013) 29(4) *Arbitration International*, p. 579; Jan Paulsson and Georgios Petrochilos, ‘Revision of The UNCITRAL Arbitration Rules’ (Freshfields Bruckhaus Deringer 2006), paras. 172-75.

⁴⁹ De Nanteuil (n 10), pp. 385-86.

Notably, in *Saluka*, which was decided before the 2010 revision of the rules, the arbitral tribunal found that this admissibility requirement – that a counterclaim be closely connected to the primary claim – constituted a “general legal principle” (see **Figure 15** below). In *Oxus*, which was decided after the 2010 revision of the rules, the arbitral tribunal still required that the counterclaim be closely connected to the primary claim, following the approach in *Saluka* (see **Figure 15** below).

Caselaw	Analysis of the Tribunal
<p><i>Saluka Investments B.V. v. The Czech Republic</i>, UNCITRAL, Decision on Jurisdiction over the Czech Republic’s Counterclaim dated 7 May 2004</p>	<p>“In relation specifically to counterclaims, it is necessary that they must also satisfy those conditions which customarily govern the relationship between a counterclaim and the primary claim to which it is a response. In particular, a legitimate counterclaim must have a close connection with the primary claim to which it is a response.” (para. 61)</p> <p>“[T]he Tribunal is satisfied that those provisions, as interpreted and applied by the decisions which have been referred to, reflect a general legal principle as to the nature of the close connection which a counterclaim must have with a primary claim if a tribunal with jurisdiction over the primary claim is to have jurisdiction also over the counterclaim.” (para. 76)</p>
<p><i>Oxus Gold v. Republic of Uzbekistan</i>, UNCITRAL, Final Award dated 17 December 2015</p>	<p>“For the Arbitral Tribunal to have jurisdiction over the counterclaims, it is necessary that there be a close connection between them and the primary claim from which they arose in the sense that the counterclaims must be sufficiently connected to the claims, i.e. arise out of the investment and thereto relating obligations, and may not be matters merely covered by the general law of the Respondent.” (para. 954)</p>

Figure 15: Relevant UNCITRAL cases discussing the connection requirement

As a result, even under the revised UNCITRAL Arbitration Rules, the connection requirement must be satisfied for a counterclaim to be considered admissible, despite Article 21(3) no longer expressly requiring it.⁵⁰

2.3 Key Findings

The discussion on consent and admissibility under the ICSID Convention and the ICSID Arbitration Rules as well as under the UNCITRAL Arbitration Rules provides important findings that must be considered when drafting a counterclaim provision.

In relation to **jurisdiction (i.e. the consent requirement)**:

- ICSID and UNCITRAL provide similar requirements regarding consent;
- Consent concerning counterclaims can be implied or express;

⁵⁰ Ishikawa (n 3), pp. 88-9.

- A broad dispute resolution provision, that leaves room for implied consent, makes it more likely that a counterclaim will be heard by an arbitral tribunal;
- Modern international investment agreements no longer rely on implied consent and provide for express consent of the parties (*see* **Section 5.1**).

In relation to **admissibility** (*i.e.* **connection requirement**):

- While the ICSID Convention specifically prescribes a connection between a state counterclaim and the investor's primary claim, the current UNCITRAL Arbitration Rules no longer refer to a connection requirement. However, recent caselaw indicates that – even under the revised UNCITRAL Arbitration Rules – tribunals investigate whether a connection between the counterclaim and the primary claim exists;
- The connection between a state counterclaim and the investor's primary claim can be either legal or factual. Tribunals' interpretations of the connection requirement and recent treaty practice addressing this issue are inconsistent. The report finds that it is easier to establish a factual than a legal connection between a counterclaim and the primary claim;
- The caselaw reveals that tribunals enjoy a wide margin of discretion when establishing admissibility. This report finds that tribunals might be willing to move away from a strict legal connection requirement and consider a factual connection as solely sufficient.

3 Applicable Law and Investor Obligations

The parties' choice (or lack thereof) of the law applicable to the merits of the dispute plays a decisive role in relation to any counterclaims that a host state may raise against the investor. In some cases, the law applicable to the counterclaims will be the same as the law applicable to any claims raised by the investor; in other cases, the parties may opt for (or the tribunal may apply) a separate body of law to state counterclaims. Similarly, the parties' choice as to whether to incorporate any direct investor obligations in the investment agreement or to import these obligations from other sources of law applicable to the merits of the dispute is also pivotal to the success of a state counterclaim. **Section 3.1** will consider the impact that the varying choices of applicable law may have on the success of a state counterclaim. **Section 3.2** delves into the question of investor obligations.

3.1 **Applicable Law**

The report focuses on questions of applicable law under the ICSID Convention and the UNCITRAL Arbitration Rules.

3.1.1 **Applicable Law under the ICSID Convention**

Article 42(1) of the ICSID Convention is the core provision for determining the law applicable to the merits of a dispute (*see* **Figure 16** below).

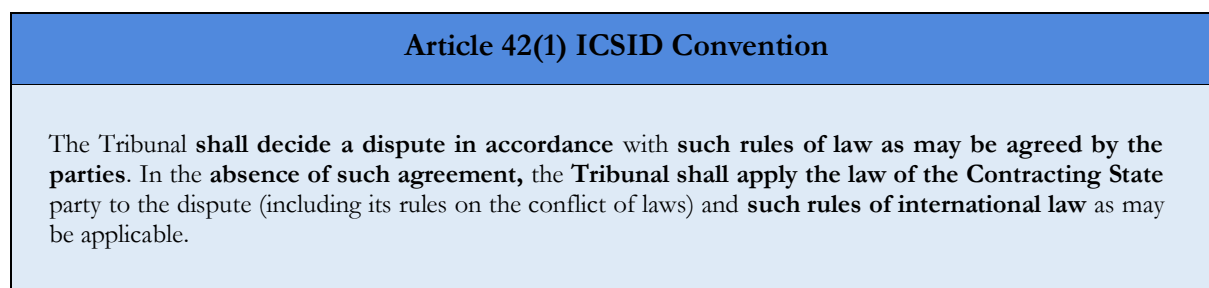


Figure 16: Article 42(1) of the ICSID Convention

Article 42(1) provides that the law applicable to the merits of the dispute consists of the set of rules agreed by the parties. In the absence of an agreement, Article 42(1) requires the tribunal to apply the host state's law (including its conflict of law rules) and any applicable rules of international law.⁵¹

⁵¹ Dolzer, Kriebaum and Schreuer (n 1), pp. 416-17.

3.1.1.1 Agreement on Applicable Law

The parties can agree on the law governing a treaty-based investment dispute, including any counterclaims raised by a state against the investor, by inserting a specific provision in the investment agreement. Applicable law provisions vary in scope. Typically, one or a combination of the following bodies of law can be chosen as applicable law:⁵²

1. the law of the host state (domestic law);
2. the domestic law of another state (*i.e.* the home state or a third state not party to the investment agreement/dispute);⁵³
3. international law (*i.e.* international law designated by the investment agreement, customary international law and the general principles of international law); and/or
4. the law of the underlying contract.⁵⁴

The investor accepts the law designated by the parties for application to the merits of the dispute by raising a claim based on the dispute resolution provision.⁵⁵ When an applicable law provision includes several bodies of law without prioritizing them (which is common in treaty practice), tribunals have the discretion to determine the law applicable to the dispute.⁵⁶

3.1.1.2 No Agreement on Applicable Law

In the absence of an agreement on the law applicable to the merits of the dispute, Article 42(1) prescribes that the tribunal must apply the domestic law of the host state (including its conflict of law rules) and rules of international law that “may be applicable”.⁵⁷ The use of the word “may” indicates that tribunals retain a certain discretion as to what rules of international law could apply to the merits of the dispute.⁵⁸

⁵² Dolzer, Kriebaum and Schreuer (n 1), p. 418: *e.g.* Article 1131 NAFTA: “A Tribunal established under this Section shall decide the issues in dispute in accordance with this Agreement and applicable rules of international law”; Article 26(6) ECT: “A tribunal established under paragraph (4) shall decide the issues in dispute in accordance with this Treaty and applicable rules and principles of international law”.

⁵³ *Southern Pacific Properties (Middle East) Limited v. Arab Republic of Egypt*, ICSID Case No. ARB/84/3, Award (20 May 1992), para. 225; *Azpetrol International Holdings B.V., Azpetrol Group B.V. and Azpetrol Oil Services Group B.V. v. Republic of Azerbaijan*, ICSID Case No. ARB/06/15, Award (8 September 2009), paras. 49-65.

⁵⁴ Schill (n 11), pp. 814-55.

⁵⁵ Dolzer, Kriebaum and Schreuer (n 1), p. 417.

⁵⁶ Jeswald W. Salacuse, *The Law of Investment Treaties* (Oxford University Press 2021), p. 530.

⁵⁷ Kjos, *Applicable Law* (n 17), p. 229.

⁵⁸ *Id.* at p. 228.

Moreover, when the investment agreement does not contain an applicable law provision, tribunals may also consider other instruments in which the parties may have indicated their choice on the applicable law, including a separate agreement between the parties.⁵⁹

3.1.2 Applicable Law under the UNCITRAL Arbitration Rules

Article 35(1) of the UNCITRAL Arbitration Rules (*see* **Figure 17** below) follows the two-step approach of Article 42(1) of the ICSID Convention.

Article 35(1) UNCITRAL Arbitration Rules
The arbitral tribunal shall apply the rules of law designated by the parties as applicable to the substance of the dispute. Failing such designation by the parties, the arbitral tribunal shall apply the law which it determines to be appropriate .

Figure 17: Article 35(1) of the UNCITRAL Arbitration Rules

First, the tribunal must apply the law agreed upon by the parties. Second, in the absence of such an agreement, the tribunal applies the “the law which it determines to be appropriate”.

3.1.2.1 Agreement on Applicable Law

Similarly to Article 42(1) of the ICSID Convention, Article 35(1) of the UNCITRAL Arbitration Rules favors parties’ autonomy by requiring the tribunal to apply the law of their choice (*see* discussion in **Section 3.1.1**).⁶⁰ The wording “rules of law” allows for the parties to choose specific sources of law rather than committing to an entire legal system.⁶¹

3.1.2.2 No Agreement on Applicable Law

When there is no agreement on the applicable law, the choice is left to tribunals. Unlike Article 42(1) of the ICSID Convention, Article 35(1) of the UNCITRAL Arbitration Rules makes no reference to the host state’s law, international law, nor to conflict of law rules. This lack of specification indicates a more tribunal-centric approach whereby tribunals have substantial

⁵⁹ Other examples include domestic legislation containing applicable law provisions, the pleadings of the parties, treaties in force between the parties as a source of international law. Schill (n 11), pp. 829-31. *See Asian Agricultural Products Ltd. v. Republic of Sri Lanka*, ICSID Case No. ARB/87/3, Final Award (27 June 1990), para. 20 – for party pleadings used by the tribunal to determine the applicable law. *See also MTD Equity Sdn. Bhd. and MTD Chile S.A. v. Republic of Chile*, ICSID Case No. ARB/01/7, Award (25 May 2004), para. 87 – where the tribunal rejected the idea that the second part of Article 42(1) of the ICSID Convention applies when there is no applicable law provision in the treaty, and instead concluded that, because the instrument was a treaty, the tribunal was required to apply international law.

⁶⁰ Caron and Caplan (n 40), p. 114.

⁶¹ Kjos, *Applicable Law* (n 17), p. 231.

discretion to determine the law that they consider “appropriate” for application to the merits of the dispute.⁶²

3.1.3 Counterclaims and Tribunals’ Interpretation of Applicable Law Provisions

Tribunals have addressed questions of applicable law mainly when assessing the merits of counterclaims. **Figure 18** illustrates the effect that applicable law provisions in investment agreements may have on the determination of the merits of a counterclaim. It equally illustrates that applicable law provisions may provide for external grounds – outside the four-corners of the investment agreement – from which investor obligations can be sourced and upon which, in turn, states can base their counterclaims.

Caselaw	Applicable Law Provision	Analysis of the Tribunal
<p><i>Saluka Investments B.V. v. The Czech Republic</i>, UNCITRAL Decision on Jurisdiction over the Czech Republic’s Counterclaim dated 7 May 2004</p>	<p>Article 8 Czech Republic–Netherlands BIT</p> <p>(6) The arbitral tribunal shall decide on the basis of the law, taking into account in particular though not exclusively:</p> <ul style="list-style-type: none"> • the law in force of the Contracting Party concerned; • the provisions of this Agreement, and other relevant Agreements between the Contracting Parties; • the provisions of special agreements relating to the investment; • the general principles of international law. 	<p>“Moreover, by Article 8(6) of the Treaty the Tribunal is required, in reaching its decision, to take into account inter alia “the provisions of special agreements relating to the investment.” Given the facts of this arbitration, the Share Purchase Agreement, including its Article 21, constitutes a special agreement relating to Saluka’s investment. It follows that the Tribunal is required by the terms of the Treaty to take into account the mandatory arbitration provision in Article 21 of that Agreement. (para. 56)</p> <p>“As regards the requirement of a close connection between a counterclaim and the primary claim, the Tribunal notes that the parties have nowhere suggested that such a connection is not required by any of the legal bases on which, under Article 8(6) of the Treaty, it is to take its decision, including Czech law.” (para. 62)</p>
<p><i>Urbaser v. Argentina</i>, ICSID Case No. ARB/07/26, Award dated 8 December 2016</p>	<p>Article X Argentina–Spain BIT</p> <p>(5) The arbitral tribunal shall make its decision on the basis of this Agreement and, where appropriate, on the basis of other treaties in force between the Parties, the domestic law of the Party in whose territory the investment was made, including its norms of private international law, and the general principles of international law.</p>	<p>The tribunal held that Article X(5) “instructs the Tribunal to make its decision on the basis of the BIT and, where appropriate, by reference to one of the two bases other than the host State’s domestic law, which are the main sources of international law, i.e. ‘other treaties in [force] between the Parties’ and ‘general principles of international law’.” (para. 1201)</p>

Figure 18: Relevant counterclaim cases discussing applicable law provisions

⁶² Caron and Caplan (n 40), pp. 124-25.

For example, in *Saluka*, the tribunal noted that the applicable law provision at Article 8(6) included domestic law as well as “provisions of special agreements relating to the investment”.⁶³ This allowed the Czech Republic to file a counterclaim based on domestic law breaches as well as contractual breaches. However, the tribunal ultimately dismissed the counterclaims as it considered that the Czech Republic should refer its counterclaims to the forum mentioned in the special agreement.⁶⁴ In *Urbaser*, the tribunal noted that the applicable law provision at Article X(5) covered, in addition to the BIT, “other treaties in force between the Parties” and “general principles of international law”.⁶⁵ This, in turn, allowed Argentina to base its counterclaim on international law and “the human right to water contained therein”,⁶⁶ although the counterclaim was ultimately dismissed on the merits (*see Section 3.2.4* below).

Applicable law provisions give host states some degree of certainty as to the rules that a tribunal will consider when deciding the merits of a dispute, including their counterclaims. States that do not want arbitral tribunals to interpret their domestic law can choose to exclude domestic law from the applicable law provision. It should be noted, however, that, in some cases,⁶⁷ arbitral tribunals have bypassed these limitations.⁶⁸ In relation to counterclaims, applicable law provisions are also important to determine the scope of investor obligations, which, in turn, may form the basis of state counterclaims.⁶⁹

3.2 Investor Obligations

A key consideration by tribunals when assessing counterclaims is whether an investor has breached an obligation imposed upon it. The report identifies four main sources of investor obligations: (i) the investment agreement, (ii) the underlying investment contract, (iii) domestic law, and (iv) international law (*see Figure 19* below).⁷⁰ States are free to include any, some, or all of these sources in an applicable law provision, and this choice reduces or expands the scope of the investor obligations that can be invoked, which demonstrates the importance of carefully drafting applicable law provisions in investment agreements.

⁶³ *Saluka v. Czech Republic* (n 33), para. 56.

⁶⁴ *Id.* at para. 57.

⁶⁵ *Urbaser v. Argentina* (n 28), para. 1201.

⁶⁶ *Id.* at para. 1157.

⁶⁷ *See e.g. Libananco Holdings Co Limited v. Turkey*, ICSID Case No. ARB/06/8, Award (2 September 2011), para. 112, where the tribunal applied domestic law to the merits of the claim despite the fact that the relevant applicable law provision only referred to international law. This case, however, did not relate to a counterclaim.

⁶⁸ Christoph Schreuer, ‘Jurisdiction and Applicable Law in Investment Treaty Arbitration’, (2014) 1(1) McGill Journal of Dispute Resolution, pp. 18-20.

⁶⁹ De Nanteuil (n 10), pp. 381-84.

⁷⁰ Yarasalu Kryvoi, ‘Counterclaims in Investor-State Arbitration’ (2012) 21(2) Minnesota Journal of International Law, pp. 235-36.

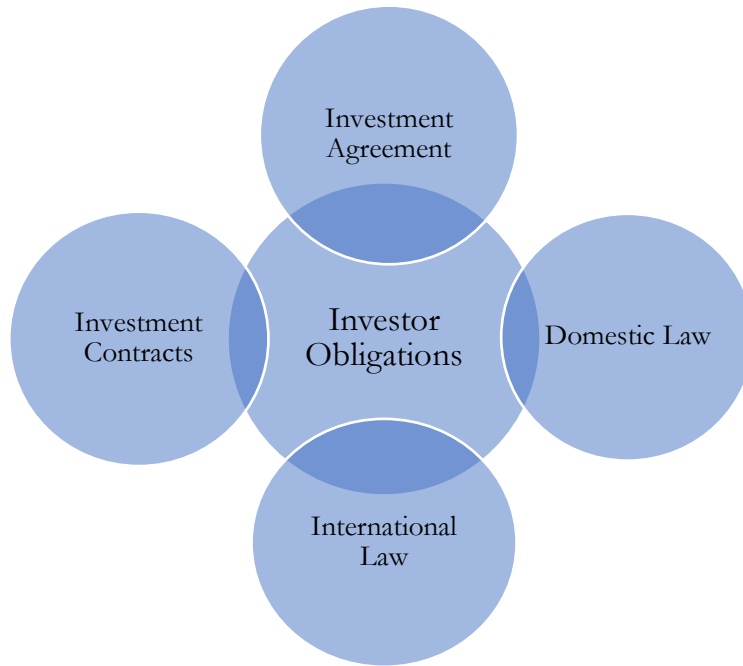


Figure 19: Illustration of the different sources of investor obligations

3.2.1 Investor Obligations in Investment Agreements

Traditionally, investment agreements abstained from imposing obligations on investors. Modern or revised investment agreements, however, have started to expressly incorporate direct investor obligations, such as obligations to comply with the domestic laws of the host state, to respect human rights, to operate the investment in accordance with environmental standards, or to adopt socially responsible practices^{71, 72}.

The express inclusion of direct investor obligations in modern investment agreements strengthens the position of host states willing to submit a counterclaim.⁷³ When direct investor obligations are not expressly codified in an investment agreement, they may – at least in principle – be able to be imported via other provisions in the investment agreement, namely (a) umbrella clauses (*see Section 3.2.1.1* below), and (b) environmental (and other) exceptions (*see Section 3.2.1.2* below).

⁷¹ A comprehensive list of the investor obligations codified in the agreements reviewed in this report is provided in **Appendix 2**.

⁷² Martin Jarrett, Sergio Puig, Steven Ratner, 'Towards Greater Investor Accountability: Indirect Actions, Direct Actions by States and Direct Actions by Individuals' (2021) 14(2) *Journal of International Dispute Settlement*, p. 1.

⁷³ *Ibid.* See also Laurent Gouiffès and Melissa Ordonez 'Climate Change in International Arbitration, the Next Big Thing?' (2022) 40(2) *Journal of Energy & Natural Resources Law*, p. 221.

3.2.1.1 Investor Obligations Sourced via Umbrella Clauses

Umbrella clauses are standards of protection that bring non-treaty commitments of the parties, including obligations stipulated in the underlying investment contract, under the protection of the investment agreement.⁷⁴ These clauses are included in an investment agreement to ensure that host states uphold any obligations they have entered into in relation to investments covered by the agreement.⁷⁵ **Figure 20** below provides an example of a standard umbrella clause.⁷⁶

Article 10(2) Philippines/Switzerland BIT
Each Contracting Party shall observe any obligation it has assumed with regard to specific investments in its territory by investors of the other Contracting Party.

Figure 20: Example of a standard umbrella clause

There is a great variation in the wording of umbrella clauses in both old and modern investment agreements. Notably, in modern investment agreements, states tend to reduce the scope of application of these clauses and exclude investment contracts and/or domestic law.⁷⁷ Some of the newer investment agreements go even further and do not even include an umbrella clause.⁷⁸

The report investigates whether an umbrella clause may, in and of itself, serve to source an investor obligation upon which a counterclaim can be based. So far, tribunals have denied this possibility.

In *Roussalis v. Romania*, for example, the majority of the tribunal interpreted the wording of the umbrella clause at Article 2(6) of the Greece/Romania BIT as a confirmation that the host state, and the host state only, “commit[ted] itself to comply with obligations it [...] entered into with regard to investments of investors” (see **Figure 21** below). The majority of the tribunal thus concluded that the umbrella clause at Article 2(6) “d[id] not permit that claims be brought about obligations of the investor”.⁷⁹

⁷⁴ Dolzer, Kriebaum and Schreuer (n 1), p. 272.

⁷⁵ Salacuse (n 56), p. 367.

⁷⁶ Dolzer, Kriebaum and Schreuer (n 1), p. 272.

⁷⁷ European Parliament, Policy department, ‘Study: The Investment Chapters of the EU’s International Trade and Investment Agreements in a Comparative Perspective’ (2015), para. 15.19.

⁷⁸ UNCTAD, ‘IIA Issues Note, International Investment Agreements, Review of ISDS Decisions in 2019: Selected IIA Reform Issues’ (January 2021); UNCTAD, ‘Mapping of IIA clauses’ available at <https://investmentpolicy.unctad.org/pages/1031/mapping-of-iiia-clauses/> accessed 10 December 2022; Raul Pereira de Souza, ‘Closing the Umbrella: A Dark Future for Umbrella Clauses’ (Kluwer Arbitration Blog, 13 October 2017).

⁷⁹ *Roussalis v. Romania* (n 16), para. 875.

In *Oxus v Uzbekistan*, the tribunal reached a similar conclusion on similar grounds. Relevantly, it held that the umbrella clause at Article 2(2) of the UK/Uzbekistan BIT “expressly refer[red] to obligations of the host State only”; it also concluded that, for these reasons, Uzbekistan could “not rely on the umbrella clause to transform a breach of contract by Claimant into a breach of the BIT” upon which Uzbekistan’s counterclaim could be based (see **Figure 21** below). Thus, in both cases, the tribunals did not permit the use of the relevant umbrella clause to elevate contractual obligations of the investor upon which a counterclaim could be based to the investment treaty plane. This interpretation is consistent with the traditional understanding of umbrella clauses as a one-sided protection for investors.⁸⁰

Caselaw	Relevant Provision	Analysis of the Tribunal
<p><i>Roussalis v. Romania</i>, ICSID Case No. ARB/06/1, Award dated 7 December 2011 and Declaration dated 28 November 2011</p>	<p>Article 2 Greece–Romania BIT</p> <p>(6) Each Contracting Party shall observe any other obligation it may have entered into with regard to investments of investors of the Contracting Party.</p>	<p>The majority of the tribunal held that “[p]ursuant to the interpretation rules of Article 31 of the Vienna Convention, the reference in the text of Article 2(6) of the BIT to “any other obligation [...] with regard to investments of investors” confirms that the host State commits itself to comply with obligations it has entered into with regard to investments of investors. It does not permit that claims be brought about obligations of the investor.” (para. 875)</p>
<p><i>Oxus Gold plc v. Republic of Uzbekistan</i>, UNCITRAL, Final Award dated 17 December 2015</p>	<p>Article 2 UK–Uzbekistan BIT</p> <p>(2) [...] Each Contracting Party shall observe any obligation it may have entered into with regard to investments of nationals or companies of the other Contracting Party.</p>	<p>“Respondent has not convincingly established that the non-payment of Claimant’s debt under this Agreement constitutes more than a mere contractual breach subject to Uzbek law. In particular, a recourse to the umbrella clause of the BIT is not possible given the wording of such clause, which expressly refers to obligations of the host State only. Thus, Respondent may not rely on the umbrella clause to transform a breach of contract by Claimant into a breach of the BIT. Therefore, it is not clear how the non-performance of this contractual undertaking would trigger a liability of Claimant under international law.” (para. 958.(i))</p>

Figure 21: Relevant cases where tribunals denied the possibility to source investor obligations via an umbrella clause

In sum, it is hard for a host state to use an umbrella clause as a legal basis for a counterclaim; this is due to the fact that, traditionally, these clauses have been used by tribunals to hold states liable

⁸⁰ Salacuse (n 56), p. 367.

for their actions under contractual obligations.⁸¹ Moreover, even if a state is able to rely on an umbrella clause to form the cause-of-action for a counterclaim, there are additional challenges associated with sourcing investor obligations from contracts (*see* **Section 3.2.2** below) or even domestic laws (*see* **Section 3.2.3** below).

3.2.1.2 Investor Obligations Sourced via Environmental (and Other) Exceptions

In the absence of direct investor obligations in an investment agreement, it may also be possible for a state to source investor obligations via another provision in the investment agreement, namely an exception covering environmental (or other) measures. This point was raised in *Aven v. Costa Rica*, where the tribunal considered whether the exceptions at Articles 10.11 and 10.9.3(c) of the DR-CAFTA “contain[ed], at least implicitly, some obligations to investors, especially with respect to the environmental laws of the host state” (*see* **Figure 22** below).⁸²

Caselaw	Relevant Provision	Analysis of the Tribunal
<p><i>David R. Aven and Others v. Republic of Costa Rica</i>, ICSID Case No. UNCT/15/3, Award dated 18 September 2018</p>	<p>Article 10.11 DR-CAFTA BIT</p> <p>Nothing in this Chapter shall be construed to prevent a Party from adopting, maintaining, or enforcing any measure otherwise consistent with this Chapter that it considers appropriate to ensure that investment activity in its territory is undertaken in a manner sensitive to environmental concerns.</p> <p>Article 10.9.3 of the DR-CAFTA</p> <p>(c) Provided that such measures are not applied in an arbitrary or unjustifiable manner, and provided that such measures do not constitute a disguised restriction on international trade or investment, [...] shall not be construed to prevent a Party from adopting or maintaining measures, including environmental measures [...]</p>	<p>“A logical effect of Article 10.11 could be that the “measures” adopted by the host State for the protection of the environment should be deemed to be compulsory for everybody under the jurisdiction of the State, particularly the foreign investors. Therefore, following said interpretation the investors have the obligation, not only under domestic law but also under Section A of Chapter 10 of DR-CAFTA to abide and comply the environmental domestic laws and regulations, including the measures adopted by the host State to protect human, animal, or plant life or health.” (para. 734)</p>

Figure 22: *Aven v. Costa Rica*

⁸¹ See e.g. *LG&E Energy Corp., LG&E Capital Corp., and LG&E International, Inc. v. Argentine Republic (LG&E v. Argentina)*, ICSID Case No. ARB/02/1, Decision on Liability (3 October 2006); *Noble Ventures Inc. v. Romania*, ICSID Case No. ARB/01/11, Award (12 October 2005).

⁸² *Aven v. Costa Rica* (n 3), para. 732.

In *Aven*, the tribunal found that Article 10.11 recognized Costa Rica's right to adopt measures for the protection of the environment which, once adopted, would impose obligations upon everyone, including foreign investors.⁸³ In the words of the tribunal, "no investor can ignore or breach [...] measures [adopted by the host State for the protection of the environment] and its breach is a violation of both domestic and international law, so that the perpetrator cannot be exempt of liability for the damages caused".⁸⁴ Following the analysis of the dispute resolution provisions at Articles 10.15 and 10.16 of the DR-CAFTA, the tribunal concluded that their language was "wide enough to encompass counterclaims". As a result, the tribunal held that it had *prima facie* jurisdiction over Costa Rica's counterclaims against the investor.

Relevantly, however, the tribunal stated that the environmental exceptions at Articles 10.11 and 10.9.3(c), while recognizing host states' right to regulate to protect the environment, did not go as far as imposing "in and of themselves— [...] any affirmative obligations upon investors" to protect the host state's environment.⁸⁵ In this sense, the tribunal considered that Articles 10.11 and 10.9.3(c) did not create a presumption that "any violation of state-enacted environmental regulations [would] amount to a breach of the Treaty which could be the basis of a counterclaim".⁸⁶ From this follows that, while a counterclaim can be based on the breach of an environmental measure, it is not enough for the host state to show that the investor did not comply with its environmental measures; in the tribunal's view, the host state must also show that the investor breached other substantive obligations reflected in the investment agreement.

While seemingly progressive, the tribunal's conclusion appears tautological, as either when an investor violates a host state's measure adopted to protect the environment it also violates both its domestic law and international law as imported via the environmental exception, or it does not; requiring a host state to demonstrate that the investor's violation of an environmental measure also breaches some other substantive obligation in the investment agreement is equivalent to denying that the investor's violation of an environmental measure also amounts to a breach of the investment agreement. For this reason, this case, while in principle opening the door to counterclaims based on investor obligations sourced via exceptions covering environmental (and other) measures, it does not go as far as establishing this in practice.

⁸³ *Id.*, para. 734.

⁸⁴ *Id.* at para. 734.

⁸⁵ *Id.* at para. 743.

⁸⁶ *Id.* at para. 743.

3.2.2 Investor Obligations Directly Sourced from Contracts

Contracts between the host state and the investor – such as development contracts, public service concessions, and tax stabilization agreements – frequently contain substantive investor obligations which, in principle, could form the basis of a state counterclaim.⁸⁷ The report identifies two circumstances in which a contractual breach may form the basis of a counterclaim: (1) when the contractual breach can be elevated to a treaty breach by an umbrella clause (see **Section 3.2.1.1** above);⁸⁸ (2) when the breach relates to a provision of a contract related to the investment, provided that the relevant dispute resolution provision in the investment agreement is drafted broadly enough as to encompass contract-based counterclaims. Both circumstances, however, are difficult to materialize in practice.

Arbitral tribunals have been cautious in entertaining both claims and counterclaims based on contractual obligations. In relation to claims based on contractual obligations, tribunals have generally abstained from adjudicating contractual breaches and have, instead, opted to ‘give effect to any valid choice of forum clause in the contract’.⁸⁹ In the same vein, tribunals have generally abstained from adjudicating a counterclaim based on a contractual breach, especially when the contract at issue contained a separate forum resolution clause. This was the case in *Saluka v Czech Republic* and in *Oxus v Uzbekistan*, where tribunals dismissed a contract-based counterclaim on the grounds that the contract contained its own dispute resolution clause (see **Figure 23** below).

Caselaw	Analysis of the Tribunal
<p><i>Saluka v. Czech Republic</i>, UNCITRAL Decision on Jurisdiction over the Czech Republic’s Counterclaim dated 7 May 2004</p>	<p>“By Article 8(6) of the Treaty the Tribunal is required, in reaching its decisions, to take into account inter alia “the provisions of special agreements relating to the investment.” Given the facts of this arbitration, the Share Purchase Agreement, including its Article 21, constitutes a special agreement relating to Saluka’s investment. It follows that the Tribunal is required by the terms of the Treaty to take into account the mandatory arbitration provision in Article 21 of that Agreement.” (para. 56)</p> <p>“The Tribunal thus cannot in this arbitration entertain a counterclaim based on a dispute arising out of or in connection with, or the alleged breach of, an agreement which both contains its own mandatory arbitration provision and is an agreement which the Tribunal is expressly required to take into account.” (para. 57)</p>

⁸⁷ Salacuse (n 56) p. 363; Kjos, *Applicable Law* (n 17), pp. 134-35.

⁸⁸ Ignacio Tortorola, Gary J. Shaw and Bethel Kassa, ‘Chapter 24: Opening the Umbrella: How the Argentine Economic Crisis Cases Shaped the Modern Umbrella Clause’ in Fabricio Fortese (ed), *Arbitration in Argentina* (Kluwer Law International 2020), pp. 349-50.

⁸⁹ *Compañía de Aguas del Aconquija S.A. and Vivendi Universal S.A. v. Argentine Republic*, ICSID Case No. ARB/97/3, Decision on Annulment (3 July 2002), para 98. See also Dolzer, Kriebaum and Schreuer (n 1), p. 394; Pierre Lalive and Laura Halonen, ‘On the Availability of Counterclaims in Investment Treaty Arbitration’ in AJ Bělohávek and Rozeh N (eds), *Czech Yearbook of International Law* (Juris 2011), p. 151.

<p><i>Oxus Gold v. Republic of Uzbekistan</i>, UNCITRAL, Final Award dated 17 December 2015</p>	<p>“Under such circumstances, even if the SDA counterclaims would be seen as falling under the scope of Article 8(1) of the BIT, the Arbitral Tribunal considers that the forum selection clause contained in Article 9 of the Special Dividend Agreement constitutes a special agreement between the Parties by which they provided for a specific dispute resolution mechanism [...]. In other words, this special dispute resolution clause constitutes a sort of carve-out from a potential jurisdiction under the BIT and deprives the Arbitral Tribunal of any jurisdiction over such counterclaims.” (para. 958)</p>
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Figure 23: Relevant cases where tribunals dismissed contract-based counterclaims

These cases are helpful to understand arbitral tribunals’ reasoning in relation to contract-based counterclaims where the contract at issue provides for its own forum selection clause. These clauses are common in contracts between the host state and the investor. In the event, however, that a contract did not include such a clause, it cannot be ruled out that an arbitral tribunal may accept to hear a contract-based counterclaim.

3.2.3 Investor Obligations Directly Sourced from Domestic Law

Domestic law can, as a matter of principle, impose direct obligations on investors and, in some circumstances, be used as a valid legal basis for a state counterclaim. The most emblematic cases where an arbitral tribunal concluded that it had jurisdiction to hear counterclaims based on domestic law breaches are *Burlington v. Ecuador* and *Perenco v. Ecuador*. These cases, however, are exceptional for several reasons.

First, in both cases, the investor accepted the jurisdiction of the arbitral tribunal over the counterclaims: while Burlington concluded a separate agreement with Ecuador on this point, Perenco was found to have implicitly accepted the tribunal’s jurisdiction over Ecuador’s counterclaims. In addition, both Burlington and Perenco did not dispute that domestic law (*i.e.* Ecuadorian law) would apply to the substance of the dispute (*see* **Figure 24** below).⁹⁰

Caselaw	Analysis of the Tribunal
<p><i>Burlington Resources Inc v. Republic of Ecuador</i> ICSID Case No ARB/08/5, Decision on Ecuador’s Counterclaims dated 7 February 2017</p>	<p>“Pursuant to Rule 40(2) of the ICSID Arbitration 6. Rules, Ecuador asserted two counterclaims in its Counter-Memorial on Liability of 17 January 2011. Although Burlington initially stated that it would challenge the Tribunal’s jurisdiction, the Parties later executed an agreement dated 26 May 2011 by which Burlington accepted the jurisdiction of the Tribunal over the counterclaims.” (para. 6)</p> <p>“As regards the substance of the dispute, it is undisputed that Ecuadorian law applies to both the environmental and the infrastructure counterclaims. [...]”</p>

⁹⁰ Ishikawa (n 3), pp. 117-18.

	<p>Therefore, the Tribunal will apply Ecuadorian tort law, not as the law chosen by the Parties under the first leg of Article 42(1) of the ICSID Convention, but as the law of the host State under the second leg of that provision. The relevance of this distinction is that, under the second leg, international law also “may be applicable”. Subject to any particular matter that may call for the application of international law, which will be discussed if and when it arises in the analysis, the Tribunal will thus apply Ecuadorian law to the environmental counterclaims.” (paras. 71-74)</p> <p>“With respect to the infrastructure counterclaims, Ecuador argues that Burlington’s liability for the poor condition of the infrastructure arises both under the Block 7 and 21 PSCs and under Ecuadorian law. In this regard, the PSCs contain a choice of Ecuadorian law and, accordingly, the Tribunal will apply such law (under the first leg of Article 42(1) of the ICSID Convention) as well as any relevant contractual provisions of the PSCs.” (para. 75)</p>
<p><i>Perenco Ecuador Limited v. Republic of Ecuador and Empresa Estatal Petroleos del Ecuador</i> (Petroecuador) ICSID Case No ARB/08/6, Decision on Claimant’s Application for Dismissal of Respondent’s Counterclaims dated 18 August 2017</p>	<p>“At no previous stage of the proceedings relating to Ecuador’s counterclaims has Perenco raised objections, either to the Tribunal’s jurisdiction or to the admissibility of the counterclaims. Perenco was of course aware of the counterclaims raised by Ecuador in the Burlington proceedings, admitting that it “and Burlington [...] presented a joint defense throughout the counterclaims phase”. It has raised its objection to the admissibility of Ecuador’s counterclaims only now, after more than five years of arbitrating before this Tribunal, and after the Tribunal had issued its Interim Decision [...].” (para. 44)</p> <p>“The Tribunal understands Perenco’s position that it could not have earlier raised its objection to the admissibility of Ecuador’s counterclaims based on the <i>res judicata</i> effect of the Decision on the Counterclaims rendered by the Burlington tribunal on February 7, 2017 and incorporated into the Award. This Tribunal is not, however, convinced that the Burlington tribunal’s Decision renders Ecuador’s counterclaims, the admissibility of which had not been previously challenged and on which the Tribunal ruled in its Interim Decision of August 11, 2015, now inadmissible.” (paras. 45-46)</p>

Figure 24: Relevant cases where tribunals accepted to hear counterclaims based on domestic law breaches

These cases are equally emblematic in terms of the result achieved. In fact, these are the only investment law cases where state counterclaims were successful on the merits: in *Burlington*, Ecuador was awarded \$39 million for its environmental counterclaim and a further \$2.5 million for its infrastructural counterclaim;⁹¹ in *Perenco*, Ecuador was awarded \$54 million for its environmental counterclaim.⁹²

Other than in these cases, arbitral tribunals generally abstain from entertaining claims and counterclaims concerning “rights and obligations that are applicable to legal or natural persons who are within the reach of a host State’s jurisdiction” on the grounds that these claims/counterclaims “fall to be decided by the appropriate procedures in the relevant jurisdiction”.⁹³ This approach was followed in *Saluka v. Czech Republic* and *Pausbok v. Mongolia*, where

⁹¹ *Burlington v. Ecuador* (n 15), para. 1075.

⁹² Ishikawa (n 3), p. 117; *Perenco Ecuador Ltd. v. the Republic of Ecuador (Perenco v. Ecuador)*, ICSID Case No. ARB/08/6, Award (27 September 2019), paras. 898-9 and 1023(b).

⁹³ *Amco v. Indonesia* (n 12), para. 125.

tribunals considered that the counterclaims should be heard in the relevant domestic courts since they exclusively arose out of non-compliance with domestic law (see **Figure 25** below). In both of these cases, tribunals reached this conclusion despite the fact that the relevant dispute resolution provision was wide enough to encompass counterclaims.

Caselaw	Dispute Resolution and Applicable Law Provisions	Analysis of the Tribunals
<p><i>Saluka v. Czech Republic</i>, UNCITRAL Decision on Jurisdiction over the Czech Republic’s Counterclaim dated 7 May 2004</p>	<p>Article 8 Czech Republic–Netherlands BIT</p> <p>(1) All disputes between one Contracting Party and an investor of the other Contracting Party concerning an investment of the latter [...]</p> <p>(2) Each Contracting Party consents to submit a dispute referred to in paragraph (1) of this Article to an arbitral tribunal, [...]</p> <p>(6) The arbitral tribunal shall decide on the basis of the law, taking into account in particular though not exclusively:</p> <ul style="list-style-type: none"> • the law in force of the Contracting Party concerned; [...] 	<p>“Taken at face value, and on the basis of their own terms as pleaded by the Respondent, these heads D through K of the Respondent’s counterclaim cannot be regarded as constituting (to use the language adopted in <i>Klöckner v. Cameroon</i>, above, paragraph 65) “an indivisible whole” with the primary claim asserted by the Claimant, or as invoking obligations which share with the primary claim “a common origin, identical sources, and an operational unity” or which were assumed for “the accomplishment of a single goal, [so as to be] interdependent.” The legal basis on which the Respondent has itself relied for heads D through K of its counterclaim is to be found in the application of Czech law, and involves rights and obligations which are applicable, as a matter of the general law of the Czech Republic, to persons subject to the Czech Republic’s jurisdiction. Consequently, the disputes underlying those heads of counterclaim in principle fall to be decided through the appropriate procedures of Czech law and not through the particular investment protection procedures of the Treaty.” (para. 79)</p>
<p><i>Sergei Paushok, CJSC Golden East Company and CJSC Vostokneftegaz Company v. The Government of Mongolia</i>, UNCITRAL, Award on Jurisdiction and Liability dated 29 April 2011</p>	<p>Article 6 of the Russia-Mongolia BIT:⁹⁴</p> <p>(1) Disputes between a Contracting Party and an investor of the other Contracting Party, arising from implementation of investments, [...]</p> <p>No clear applicable law provision.</p>	<p>“More importantly, the Counterclaims arise out of Mongolian public law and exclusively raise issues of non-compliance with Mongolian public law, including the tax laws of Mongolia. All these issues squarely fall within the scope of the exclusive jurisdiction of Mongolian courts.” (para. 694)</p> <p>As to counterclaims concerning violations of environmental obligations and damage for gold smuggling, “they cannot be seen as having a ‘close connection with the primary claim to which (they are) a response’. Moreover, they are clearly matters which strictly concern GEM and they all relate to subjects being the object of Mongolian legislation and regulation.” (para. 696)</p>

Figure 25: Relevant cases where tribunals dismissed state counterclaims based on domestic law

⁹⁴ The text of this BIT is available only in Russian and in Mongolian. English translation available at <https://edit.wti.org/document/show/583450e8-09c3-45dc-9e5c-14a2da0c268a> accessed 10 December 2022.

Relevantly, in *Saluka* and in *Paushok*, tribunals declined jurisdiction also on grounds that the counterclaims were not sufficiently connected with the investor’s primary claim. This demonstrates the extent to which the success of a state counterclaim depends on several aspects, including, as in these cases, admissibility grounds. The scope of the relevant applicable law provision is also relevant when determining whether a counterclaim based on a domestic law breach can be heard by an arbitral tribunal. In *Gavazzi*, the majority of the tribunal dismissed Romania’s counterclaim on the grounds that Article 8(2) of the Italy/Romania BIT⁹⁵ did “not import Romanian law as substantive law to decide claims and counterclaims”.⁹⁶

More recently, arbitral tribunals have been more permissive in authorizing state counterclaims based on domestic law to be heard and reach the merit stage.

Caselaw	Dispute Resolution and Applicable Law Provisions	Analysis of the Tribunals
<p><i>Antoine Goetz & Consorts et S.A. Affinage des Métaux v. Republic of Burundi (II)</i>, ICSID Case No. ARB/01/2, Award dated 21 June 2012</p>	<p>Article 8 of the BLEU-Burundi BIT:⁹⁷</p> <p>1. For the purposes of this article, a dispute relating to an investment is defined as a dispute concerning: ...</p> <p>b) The interpretation or application of any investment authorization granted by the authorities of the host State governing foreign investment; [...]</p> <p>5. The arbitration body shall decide on the basis of:</p> <ul style="list-style-type: none"> - The national law of the Contracting Party involved in the dispute in whose territory the investment is located, including its rules on the Conflict of Laws; [...] 	<p>The tribunal found a factual connection between the claim and the counterclaim; however, the tribunal dismissed the counterclaim on the merits because of a lack of evidence.⁹⁸ (paras. 285, 287)</p>

Figure 26: *Goetz v. Burundi (II)*

⁹⁵ See *supra* (n 25).

⁹⁶ *Gavazzi v. Romania* (n 23), para. 156.

⁹⁷ Original text in French: “1. Pour l’application du présent article, un différend relatif à un investissement est défini comme un différend concernant: [...] b) l’interprétation ou l’application de toute autorisation d’investissement accordée par les autorités de l’État hôte régissant les investissements étrangers; 5. L’organisme d’arbitrage statue sur base: - du droit national de la Partie contractante partie au litige, sur le territoire de laquelle l’investissement est situé, y compris les règles relatives aux conflits de lois”. English translation available at <https://edit.wti.org/document/show/fb3a8715-8c1a-48de-8ad7-fb2fbcdeda37> accessed 10 December 2022.

⁹⁸ Original text in French: “Le Tribunal observe en premier lieu que le Burundi n’apporte pas le moindre commencement de preuve des dommages qui lui auraient été causés de fait que le comportement d’ABC aurait porté atteinte à la concurrence et à la stabilité financière du pays. Il relève en second lieu que le manque à gagner dont se plaint le Défendeur en ce qui concerne la perception de droits et taxes n’a pas pour cause la méconnaissance par ABC des obligations qui lui avaient été imposées par le certificat de zone franche. La demande reconventionnelle du Burundi doit par suite être écartée”.

In *Goetz v. Burundi (II)*, the tribunal considered both the relevant dispute resolution and applicable law provisions sufficiently broad as to cover counterclaims arising from domestic law breaches; in the end, however, it dismissed the counterclaims for lack of evidence (see **Figure 26** above).

Caselaw	Dispute Resolution and Applicable Law Provisions	Analysis of the Tribunal
<p><i>Tethyan Copper Company Pty Limited v. Islamic Republic of Pakistan</i>, ICSID Case No. ARB/12/1, Decision on Jurisdiction and Liability dated 10 November 2017</p>	<p>Article 1 of the Australia-Pakistan BIT:</p> <p>1. For the purposes of this Agreement: (a) “investment” means every kind of asset, owned or controlled by investors of one Party and admitted by the other Party subject to its law and investment policies applicable from time to time and includes: [...]</p> <p>Article 13:</p> <p>1. In the event of a dispute between a Party and an investor of the other Party relating to an investment, [...]</p> <p>2. If the dispute in question cannot be resolved through consultations and negotiations, either party to the dispute may: [...] (b) refer the dispute to the International Centre for Settlement of Investment Disputes (“the Centre”) for conciliation or arbitration ...</p> <p>Annex A:</p> <p>7. The Arbitral Tribunal shall reach its award by majority vote taking into account the provisions of this Agreement, the international agreements both Parties have concluded and the generally recognised principles of international law.</p>	<p>“... the Tribunal is of the view that, if the dispute resolution clause in a treaty allows for counterclaims, it is not for the investor to decide that such counterclaims shall not be part of its arbitration with the host State. This would contradict the intention of both the authors of the ICSID Convention and the Contracting Parties to the Treaty that the arbitration initiated by the investor should not be a “one-way street”. [...] [T]he tribunal finds that the second jurisdictional requirement is satisfied for Respondent’s counterclaim based on Article 1(1)(a) of the Treaty, [...]”. (paras. 1425-1426)</p> <p>“Respondent’s counterclaim is based on an alleged violation of Pakistani laws and investment policies and thus a lack of fulfilling the admission requirements in Article 1(1)(a) of the Treaty. [...] [T]he tribunal agrees with Claimant that Article 1(1)(a) of the Treaty cannot give rise to an obligation and a corresponding liability of the investor vis-à-vis the host State. [...] Therefore, the non-fulfillment can be invoked by the host State as a defense against claims of the investor based on a violation of any standard of protection; however, it cannot give rise to a liability of the investor for a loss of opportunity as Respondent claims. As a result, Respondent’s counterclaim based on Claimant’s alleged breach of Article 1(1)(a) of the Treaty is dismissed because this provision cannot give rise to a liability of the investor and, in any event, Claimant’s investment was admitted in accordance with Pakistani laws and investment policies at the time the investment was made in 2006.” (paras. 1441-1446)</p>

Figure 27: *Tethyan Copper v. Pakistan*

Similarly, in *Tethyan Copper v. Pakistan*, the tribunal considered that the dispute resolution provision at Article 8 of the BLEU/Burundi BIT was broad enough to cover counterclaims arising from domestic law breaches; however, it dismissed the counterclaim on the merits (*i.e.* the non-

fulfillment by the investor of investment admission requirements under Pakistani law cannot give rise to the investor's liability; *see* **Figure 27** above).⁹⁹

These cases show that, while it is possible to source investor obligations from domestic law breaches, the success of a counterclaim will depend, in practice, on jurisdictional and admissibility requirements, the scope of the relevant applicable law provision as well as, relevantly, the strength of the counterclaim on the merits. However, states intending to designate domestic law as a source of investor obligations should also consider the consequences of their domestic law being interpreted by international tribunals, as in *Burlington* and *Perenco*.

3.2.4 Investor Obligations Based on International Law

Investor obligations can also be sourced from international law, understood to cover treaties in force between the parties, customary international law and/or general principles of law/international law. Obligations based on sources of international law can provide a cause-of-action against an investor to the extent that these sources are incorporated into the investment agreement either expressly or by reference.¹⁰⁰ However, it can be argued that some obligations flowing from customary international law and general principles of law are inherently applicable to investment agreements.¹⁰¹ The different sources of international law, as illustrated in **Figure 28** below, impose different kinds of obligations upon parties, including states and investors.

⁹⁹ The other two heads of counterclaim were dismissed for lack of standing. *Tethyan Copper Company Pty Limited v. Islamic Republic of Pakistan*, ICSID Case No. ARB/12/1, Decision on Jurisdiction and Liability (10 November 2017), para. 1422.

¹⁰⁰ *See e.g. Urbaser v. Argentina* (n 28), para. 1201 holding that “Article X(5) of the BIT [...] instructs the Tribunal to make its decision on the basis of the BIT and, where appropriate, by reference to one of the two bases other than the host State’s domestic law, which are the main sources of international law, *i.e.* “other treaties in force between the Parties” and “general principles of international law”. It is thus Article X(5) itself that states the evidence that the BIT is not framed in isolation, but placed in the overall system of international law”.

¹⁰¹ *See* Laurence Boisson de Chazournes, ‘Changes in the Balance of Rights and Obligations: Towards Investor Responsabilization’ in Tarek El Ghadban, Charles-Maurice Mazuy and Alexandre Senegacnik (eds), *La Protection Des Investissements Etrangers: Vers Une Réaffirmation de l’État?/The Protection of Foreign Investments: A Reaffirmation of the State?* (Pedone 2018); Todd Weiler, ‘Balancing Human Rights and Investor Protection: A New Approach for a Different Legal Order’ (2004) 27(2) *Boston College International and Comparative Law Review*, p. 449.

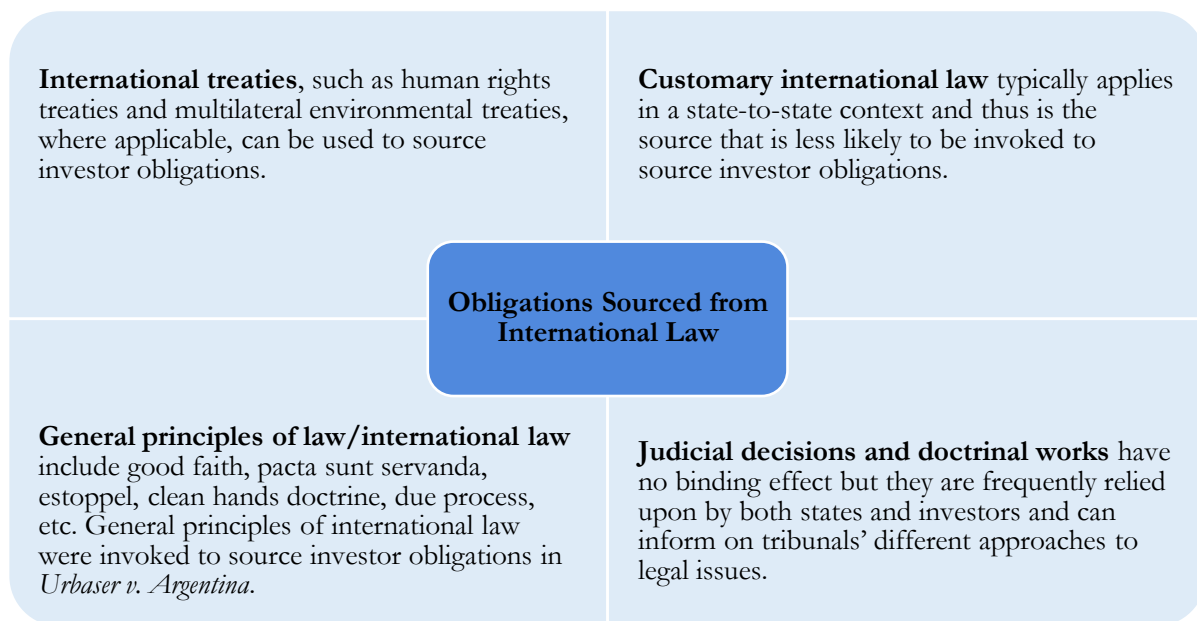


Figure 28: Obligations sourced from international law

The most emblematic cases where tribunals considered whether investor obligations could be based on international law are *Urbaser v. Argentina* and *Aven v. Costa Rica*.¹⁰² Both cases, albeit unsuccessful on the merits, are worth analyzing as they demonstrate that states can base their counterclaims on investor obligations sourced from international law, provided that the BIT contains (a) a broad dispute resolution provision and (b) an applicable law provision referring to international law.

In *Urbaser*, the tribunal interpreted the absence of an express exclusion in the dispute resolution provision of the possibility for the host state to invoke rights against an investor as a confirmation that an investment agreement can be construed as to create rights for the host State and obligations for the investor (*see Figure 29* below).¹⁰³ Furthermore, when determining whether investor obligations could be sourced exclusively from the rules of the BIT (read “in isolation”) or rather also from other applicable international law rules external to the BIT, the tribunal concluded that a BIT should “be construed in harmony with other rules of international law of which it forms part”.¹⁰⁴ This conclusion is based on an ordinary interpretation of the language of the applicable law provision at Article X(5) of the Spain/Argentina BIT, which, in addition to the BIT, expressly refers to alternative bases upon which the tribunal is instructed to take the decision, including “general principles of international law” (*see Figure 29* below). The wording of the applicable law

¹⁰² Ishikawa (n 3), pp. 118-19.

¹⁰³ *Urbaser v. Argentina* (n 28), paras. 1182-87.

¹⁰⁴ *Id.* at para. 1200.

provision and the tribunal’s reading of this provision allowed it to conclude that, in principle, Argentina could base its counterclaim on human rights rules external to the BIT.¹⁰⁵

Caselaw	Dispute Resolution and Applicable Law Provisions	Analysis of the Tribunal
<p><i>Urbaser S.A. and Consorcio de Aguas Bilbao Bizkaia, Bilbao Biskaia Ur Partzuergoa v. The Argentine Republic</i>, ICSID Case No. ARB/07/26, Award dated 8 December 2016</p>	<p>Article X of the Spain-Argentina BIT¹⁰⁶</p> <p>(1) Disputes arising between one of the Parties and an investor of the other Party concerning investments within the meaning of this Agreement shall, to the extent possible, be settled amicably between the parties to the dispute.</p> <p>(5) The arbitral tribunal shall decide on the basis of this treaty and, where appropriate, on the basis of other treaties in force between the Parties, the domestic law of the Party in whose territory the investment was made, including its rules of private international law, and the general principles of international law.</p>	<p>“The first step in the examination of the merits of Respondent’s Counterclaim is to deal with Claimants’ principled objection that the asymmetric nature of the BIT means that this Treaty does not provide for any right of the host State and, correspondingly, does not impose any obligation upon the investor. [...] A first reading of the BIT provides as answer that what Claimants assert is nowhere expressed in the BIT. [...]” (paras. 1182-1183)</p> <p>“The question is then whether any host State’s rights under the BIT shall be denied because of the very nature of BITs deemed to constitute investment law in isolation, fully independent from other sources of international law that might provide for rights the host State would be entitled to invoke and to claim before an international arbitral tribunal. [...] When assuming that the host State may not have title to rights (other than those implied in Art. IX and X) that it may invoke against an investor as holder of a corresponding obligation, the definition of a dispute able to be submitted to arbitration should carve out the possibility for the host State to invoke such rights. Interestingly, Article X(1) of the BIT does not contain such an exclusion, [...]” (paras. 1186-1187)</p> <p>The next step to undertake is then to turn to the provision on the law applicable to the Tribunal’s decision contained in Article X(5). Such decision shall be made “on the basis of this Agreement.” To this basis, the word “and” connects an additional basis, which can be, alternatively, another treaty in force between the Parties, the host State’s domestic law, or the “general principles of international law.” In order to be pertinent “where appropriate”, these additional legal bases must be connected or referred to by the</p>

¹⁰⁵ *Id.* at paras. 1188-92 and 1200-01.

¹⁰⁶ Original text in Spanish: “1. Las controversias que surgieren entre una de las Partes y un inversor de la otra Parte en relación con las inversiones en el sentido del presente Acuerdo deberán, en lo posible, ser amigablemente dirimidas entre las partes en la controversia. 5. El tribunal arbitral decidirá sobre la base del presente tratado y, en su caso, sobre la base de otros tratados vigentes entre las Partes, del derecho interno de la Parte en cuyo territorio se realizó la inversión, incluyendo sus normas de derecho internacional privado, y de los principios generales del derecho internacional”. English translation available at <https://edit.wti.org/app.php/document/show/906eff11-67f0-4fed-afb9-3f6a725b5c76> accessed 10 December 2022.

		<p>BIT (“this Agreement”), which represents the ground of the decision in all cases.” (para. 1188)</p> <p>“[...] The BIT cannot be interpreted and applied in a vacuum. The Tribunal must certainly be mindful of the BIT’s special purpose as a Treaty promoting foreign investments, but it cannot do so without taking the relevant rules of international law into account. The BIT has to be construed in harmony with other rules of international law of which it forms part, including those relating to human rights.” (para. 1200)</p>
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Figure 29: *Urbaser v. Argentina*

Despite being unsuccessful on the merits, the counterclaim raised in *Urbaser* and the discussion ensuing from it illustrate the type of international law obligations that can attach to an investor as a result of interpreting a BIT “in harmony with other rules of international law of which it forms part”.¹⁰⁷ Relevantly, the *Urbaser* tribunal rejected the notion that corporations acting as foreign investors are not capable of being duty-bearers under international law. In the words of the tribunal, it “can no longer be admitted that companies operating internationally are immune from becoming subjects of international law”.¹⁰⁸ The tribunal further found that investors can also be subject to human rights obligations, in the form of obligations not to engage in activities aimed at destroying peoples’ human rights.¹⁰⁹ The tribunal, however, clarified that whether a specific human right obligation attaches (or not) to an investor depends on the specific human right at issue.

In the case at hand, the tribunal concluded that the human right to water and sanitation clearly “entails an obligation of compliance on the part of the State” but it does not “contain an obligation for performance on [the] part of any company providing the contractually required service”.¹¹⁰ Hence, the tribunal found that, if an obligation to ensure the population’s access to water were to be placed upon an investor, such obligation would not stem from international law but rather from “the legal and regulatory environment under which the investor is admitted to operate on the basis of the BIT and the host State’s laws”.¹¹¹ The tribunal thus concluded that:

While it is thus correct to state that the State’s obligation is based on its obligation to enforce the human right to water of all individuals under its jurisdiction, this is not the case for the investors who pursue, it is true, the same goal, but on the basis of the Concession and not under an obligation derived from the human right to water. Indeed, **the enforcement of the human right to water represents an obligation to**

¹⁰⁷ *Urbaser v. Argentina* (n 28), para. 1200.

¹⁰⁸ *Id.* at para. 1195.

¹⁰⁹ *Id.* at para. 1199.

¹¹⁰ *Id.* at para. 1208.

¹¹¹ *Id.* at para. 1209.

perform. Such obligation is imposed upon States. It cannot be imposed on any company knowledgeable in the field of provision of water and sanitation services. In order to have such an obligation to perform applicable to a particular investor, a contract or similar legal relationship of civil and commercial law is required. **In such a case, the investor’s obligation to perform has as its source domestic law; it does not find its legal ground in general international law.**¹¹²

Interestingly, the tribunal also stated that the “situation would be different in case [of] an obligation to abstain, like a prohibition to commit acts violating human rights ... as [s]uch an obligation can be of immediate application, not only upon States, but equally to individuals and other private parties”.¹¹³ If upheld in future cases, this conclusion, albeit in *obiter dictum*, could have an impact on state counterclaims based on international law. In fact, if a state were to argue that the investor breached an international obligation to abstain from violating human rights (*e.g.* right to pollute the environment) and the tribunal were to follow the approach in *Urbaser*, it would be easier for the counterclaim to be successful on the merits as the threshold for showing the investor’s breach would be lower.

The possibility that an investor may be subject to obligations sourced from international law was further affirmed in *Aven v. Costa Rica*, where the tribunal endorsed the approach in *Urbaser* and stated:

it can no longer be admitted that investors operating internationally are immune from becoming subjects of international law. It is particularly convincing when it comes to rights and obligations that are the concern of all States, as it happens in the protection of the environment. It is pertinent to recall the observation of the International Court of Justice regarding this kind of obligations: “In view of the importance of the rights involved, all States can be held to have a legal interest in their protection; they are obligations *erga omnes*”.¹¹⁴

Urbaser thus confirms that investors can be subject to certain obligations based on international law.¹¹⁵

¹¹² *Id.* at para. 1210.

¹¹³ *Ibid.*

¹¹⁴ *Aven v. Costa Rica* (n 3), para. 738.

¹¹⁵ See also *Bear Creek Mining Corporation v. Republic of Peru*, ICSID Case No. ARB/14/21, Partial Dissenting Opinion of Philippe Sands (30 November 2017), para. 10: “Yet the fact that the Convention may not impose obligations directly on a private foreign investor as such does not, however, mean that it is without significance or legal effects for them. In *Urbaser v. Argentina*, (n 28), para. 1199, the Tribunal noted that human rights relating to dignity and adequate housing and living conditions “are complemented by an obligation on all parts, public and private parties, not to engage in activity aimed at destroying such rights”. The *Urbaser* Tribunal further noted that the BIT being applied in that case “has to be construed in harmony with other rules of international law of which it forms part, including those relating to human rights”, and that Article 42(1) of the ICSID Convention together with the governing law clause of that BIT (Article X(5)) provided that that “Tribunal shall apply the law of the host State and such rules of international law as may be applicable”, see para. 1200-1202.

3.3 Key findings

The discussion on the law applicable to the merits of the dispute and on investor obligations offer important findings that must be considered when drafting a counterclaim provision.

In relation to **applicable law**:

- Both Article 42(1) of the ICSID Convention and Article 35(1) of the UNCITRAL Arbitration Rules favor parties' autonomy and require tribunals to apply to the dispute the law designated by the parties in the applicable law provision. Parties can choose from a variety of sources, including international law, the domestic law of the host state (or of a third state), or the law of the underlying contract. There is a presumption that this law would also apply to any counterclaims raised by the state against the investor;
- In the absence of an agreement of the parties on the applicable law, Article 42(1) of the ICSID Convention requires tribunals to apply the law of the host state (including its conflict of law rules) and any applicable rules of international law. Article 35(1) of the UNCITRAL Arbitration Rules adopts a more tribunal-centric approach and delegates to the tribunal the determination as to what rules would be "appropriate" to adjudicate the dispute (including any counterclaims).
- While not all investment agreements contain an applicable law provision, states concerned with legal certainty are encouraged to include one and to draft it carefully as to include/exclude any sources of law which they want/do not want tribunals to use to adjudicate the dispute, including any counterclaims.

In relation to **investor obligations**:

- The cause-of-action for a counterclaim can either (a) be found in direct investor obligations stipulated in the investment agreement or (b) be sourced indirectly from the law applicable to the merits of the dispute. Old-generation investment agreements tend not to contain any direct investor obligations, but revised and modern investment agreements are progressively incorporating such obligations, thus strengthening the position of host states willing to submit a counterclaim.
- When direct investor obligations are not expressly codified in the investment agreement, they may be able to be sourced via other provisions in the investment agreement, such as (i) umbrella clauses, or, alternatively, (ii) environmental (and other) exceptions. In practice,

however, counterclaims based on investor obligations imported via an umbrella clause or an environmental exception have so far been unsuccessful.

- Similarly, in the absence of direct investor obligations in the investment agreement, these obligations may be able to be sourced indirectly from the underlying contract between the host state and the investor. In practice, however, contract-based counterclaims are also unlikely to succeed if the contract at issue contains (as is often the case) its own forum selection clause. In fact, in these circumstances, arbitral tribunals tend to give effect to such a clause and decline jurisdiction to hear the counterclaim.
- Counterclaims may also be able to be based on obligations of the investor sourced from domestic law. This is, in principle, possible insofar as the investment agreement contains (a) a broad dispute resolution provision and (b) an applicable law provision expressly referring to domestic law. So far, however, counterclaims based on domestic law breaches have been successful only in two exceptional instances, *i.e. Burlington v. Ecuador* and *Perenco v Ecuador*.
- Host states intending to designate domestic law as a source for investor obligations should also consider the consequences of their domestic law being interpreted by international tribunals. Hence, host states concerned about these consequences should explicitly exclude domestic law from the applicable law provisions within investment agreements.
- Finally, counterclaims may also be based on obligations of the investor sourced from international law. As for counterclaims based on domestic law, this is possible, in principle, insofar as the investment agreement contains (a) a broad dispute resolution provision and (b) an applicable law provision expressly referring to international law. While *Urbaser v. Argentina* and *Aven v. Costa Rica* have opened the door for the possibility of investor obligations to be sourced from international law, it should be noted that counterclaims based on international law have so far been unsuccessful.

4 UNCITRAL WG III

4.1 Background and Current Status

In 2017, UNCITRAL formally began negotiations to develop a multilateral agreement regarding procedural reforms to ISDS under UNCITRAL WG III.¹¹⁶ The resulting UNCITRAL WG III draft provisions reflect the interests of various host states and are the product of years of negotiations and compromises.¹¹⁷ The UNCITRAL WG III has also prepared a draft counterclaim provision (*i.e.* Draft Provision D) (*see* **Figure 30** below).¹¹⁸

UNCITRAL Draft Provision D
<ol style="list-style-type: none">1. The respondent may make a counterclaim:<ol style="list-style-type: none">a) arising directly out of the subject matter of the dispute; [or]b) in connection with the factual and legal basis of the claim; orc) that the claimant has breached its obligations under [this or any other applicable treaty, international law, domestic laws or investment contracts]. 2. For the avoidance of doubt, the consent of the respondent to the submission of a claim by the claimant is subject to the condition that the claimant consents to the submission of counterclaims referred to in paragraph 1.

Figure 30: UNCITRAL WG III Draft Provision D on Counterclaims

4.2 Analysis of Draft Provision D

Draft Provision D addresses several procedural hurdles associated with counterclaims.

Paragraph (1) of Draft Provision D along with Section (2) addresses the topic of jurisdiction, in particular the issue of consent. The wording “the respondent may make a counterclaim” states that

¹¹⁶ *Official Records of the General Assembly, Seventy-second Session, Supplement No. 17 (A/72/17)*, para. 264.

¹¹⁷ *See generally*, UNCITRAL Doc. A/CN.9/WG.III/WP.215. State-members include: Afghanistan (2028), Algeria (2025), Argentina (2028), Armenia (2028), Australia (2028), Austria (2028), Belarus (2028), Belgium (2025), Brazil (2028), Bulgaria (2028), Cameroon (2025), Canada (2025), Chile (2028), China (2025), Colombia (2028), Côte d’Ivoire (2025), Croatia (2025), Czechia (2028), Democratic Republic of the Congo (2028), Dominican Republic (2025), Ecuador (2025), Finland (2025), France (2025), Germany (2025), Ghana (2025), Greece (2028), Honduras (2025), Hungary (2025), India (2028), Indonesia (2025), Iran (Islamic Republic of) (2028), Iraq (2028), Israel (2028), Italy (2028), Japan (2025), Kenya (2028), Kuwait (2028), Malawi (2028), Malaysia (2025), Mali (2025), Mauritius (2028), Mexico (2025), Morocco (2028), Nigeria (2028), Panama (2028), Peru (2025), Poland (2028), Republic of Korea (2025), Russian Federation (2025), Saudi Arabia (2028), Singapore (2025), Somalia (2028), South Africa (2025), Spain (2028), Switzerland (2025), Thailand (2028), Turkey (2028), Turkmenistan (2028), Uganda (2028), Ukraine (2025), United Kingdom of Great Britain and Northern Ireland (2025), United States of America (2028), Venezuela (Bolivarian Republic of) (2028), Viet Nam (2025) and Zimbabwe (2025).

¹¹⁸ UNCITRAL Working Group III, Investor-State Dispute Settlement Reform, Forty-third session, ‘Possible Reform of Investor-State Dispute Settlement (ISDS), Draft Provisions on Procedural Reform, Note by the Secretariat’ A/CN.9/WG.III/WP.219 (11 July 2022), p. 10.

the respondent (the host state) has the right to raise a counterclaim, provided certain conditions are met. Essentially, this section provides express consent to counterclaims from the parties.

Paragraph (2) is a restatement of a generally accepted notion about investor consent in investment agreements.¹¹⁹ This refers to the principle that when an investor brings a claim based on the investment agreement's dispute settlement provision, they accept the treaty in its entirety.¹²⁰ The wording "For the avoidance of doubt" indicates that paragraph 2 aims to clarify a matter of previous caselaw. The inclusion of paragraph (2) may be the result of the controversial discussion about investors' implicit consent to counterclaims (*see* **Sections 2.1.1** and **2.2.1**). Paragraph (2) is a cautious approach ensuring the investor's consent to counterclaims.

The conditional consent in paragraph (2) ("the consent of the respondent to the submission of a claim by the claimant is subject to the condition that the claimant consents to the submission of counterclaims") is unusual as it sets a very high bar for the consent to a claim. It leaves procedural questions open as to when consent to a counterclaim is given by an investor and if a host state can withdraw consent to the claim of an investor when the investor decides not to consent to the submission of counterclaims by the host state. Moreover, the language is rather complex, which may be a function of the need to reach a compromise among the various interest groups part of the WG.

Paragraphs 1(a), 1(b), and 1(c) are connected by the word "or" and are not cumulative.¹²¹ Paragraphs 1(a) and 1(b) refer to the admissibility of counterclaims. While paragraph 1(a) replicates the wording used in Article 46 of the ICSID Convention and Rule 48 of the ICSID Arbitration Rules, paragraph 1(b) adopts the language of tribunals when interpreting the connection requirement. In practice tribunals do not agree on whether a factual and/or legal connection is required.¹²² Notably, the UNCITRAL WG III states that the pros and cons associated with option (a) and option (b) should be considered before deciding which option should be retained (either one or both).¹²³

If option 1(a) is retained, tribunals may apply different approaches based on their understanding of the language "arising out of the subject-matter of the dispute".¹²⁴ On the other hand, paragraph

¹¹⁹ Dolzer, Kriebaum and Schreuer (n 1), p. 366.

¹²⁰ *Ibid.*

¹²¹ UNCITRAL WG III (Investor-State Dispute Settlement Reform) (n 118), paras. 47-51.

¹²² *See* **Section 2.1.2**.

¹²³ UNCITRAL WG III (Investor-State Dispute Settlement Reform) (n 118), para. 48.

¹²⁴ *See* **Section 2.1.2**.

1(b) clarifies that the counterclaim should be both factually and legally connected with the investor's claim, elaborating further on the test the tribunals should apply when determining admissibility. As explained in **Section 2.1.2**, while a factual connection is easier to establish than a legal connection, a strict legal connection requirement makes it even more difficult for states to raise a counterclaim based on legal instruments other than the investment agreement itself.

Option 1(c) allows a state to file a counterclaim which is not linked to the subject-matter of the dispute or the legal or factual basis of the claim of the investor.¹²⁵ Article 46 of the ICSID Convention (“except as the parties otherwise agree”) also allows the parties to exclude these connection requirements by express agreement.¹²⁶ In practice, when determining the admissibility of a state counterclaim, tribunals have always considered whether either or all of the connection requirements exist.¹²⁷ Thus, there seems to be a general expectation that at least some connection between the claim and the counterclaim is required, as demonstrated, for example, in *Oxus*.¹²⁸ It is thus difficult to forecast how an arbitral tribunal would interpret Section 1(c) of UNCITRAL Draft Provision D.

The wording “this or any other applicable treaty, international law, domestic laws or investment contracts” provides treaty negotiators with the choice of the bodies of law from which to source investor obligations. In light of the process of modernization of investment agreements, which progressively include investor obligations (*see Appendix 2*), UNCITRAL WG III noted that:

[...] draft provision D does not aim to specify the obligations of investors. (A/CN.9/1044, para. 59). Yet, in order to raise counterclaims in treaty-based investment disputes, the substantive obligations, the breach of which would form the basis of the counterclaims, would need to be included in the respective treaty.¹²⁹

By agreeing on the law from which to source investor obligations in paragraph 1(c), host states have the possibility to instruct tribunals as to whether to apply (or not) any specific body of law, including for example, domestic law to their counterclaims.

Figure 31 showcases the different options set out in UNCITRAL Draft Provision D.

¹²⁵ UNCITRAL WG III (Investor-State Dispute Settlement Reform) (n 118), para. 49.

¹²⁶ *See Section 2.1.1.*

¹²⁷ For an in-depth discussion on the caselaw surrounding the “connection requirement” *see Sections 2.1.2 and 2.2.2.*

¹²⁸ *Oxus v. Uzbekistan* (n 44), para. 954.

¹²⁹ UNCITRAL WG III (Investor-State Dispute Settlement Reform) (n 118), para. 50.

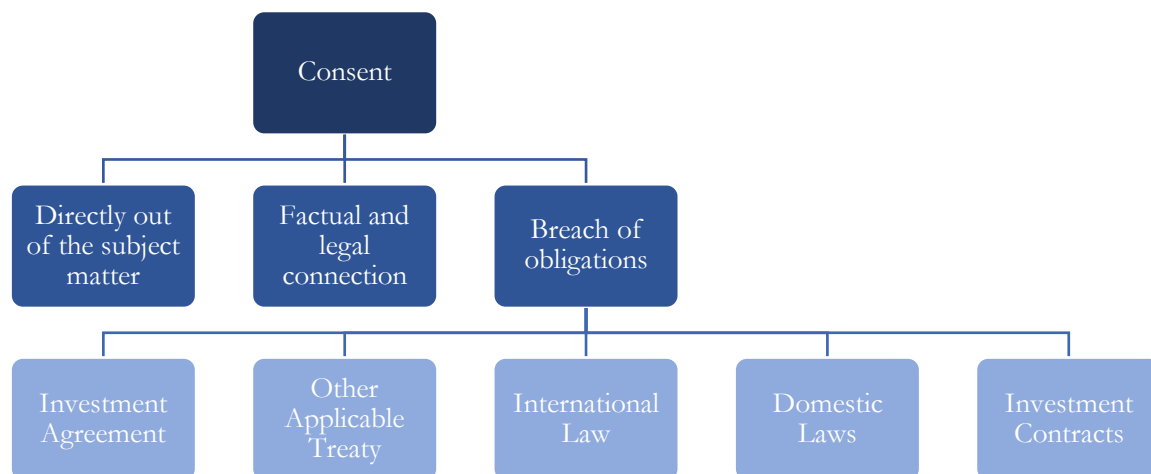


Figure 31: Flowchart of Draft Provision D

To conclude, UNCITRAL Draft Provision D proposes several reform options but does not endorse a specific methodology. The difference between the model language proposed by UNCITRAL WG III and the actual language included in investment agreements highlights the varied approaches to drafting counterclaim provisions. While some states have already determined that reforms are needed and are desirable, other states and some pro-investor groups oppose the reform as they believe the current system serves their interests well.¹³⁰ Each option has its pros and cons, as discussed above. By presenting these options together in one draft provision, the UNCITRAL Draft Provision D promotes a flexible approach, while, at the same time, does not address the practical contradictions and linguistic uncertainty arising from it. The report proposes a Model Counterclaim Provision which attempts to address some of these difficulties.

¹³⁰ Sofia Baliño, 'UN Negotiations to Reform Investor–State Arbitration Reach Critical Juncture' (IISD, 30 April 2021).

5 Model Counterclaim Provision

Building on the key findings of this report, Section 5 proposes a Model Counterclaim Provision (“Model Counterclaim Provision” or “Model Provision”) which takes UNCITRAL Draft Provision D as a starting point. This Model Provision is carefully drafted to provide parties with greater legal certainty and to curtail as much as possible the extent to which tribunals may interpret its wording at their own discretion. It does so by considering the ways in which tribunals have interpreted the wording of existing counterclaim provisions on jurisdiction, admissibility, and applicable law aspects. It also provides linguistic recommendations for treaty-drafters with a view to guide them on how to avoid common procedural hurdles or unwanted outcomes such as leaving the door open for arbitral tribunals to interpret host states’ domestic law. The Model Provision achieves this objective by giving treaty-drafters the flexibility to determine the bodies of law applicable to the merits of the counterclaim. The Model Provision is presented below (see **Figure 32** below).

Model Counterclaim Provision
<p>1. When an investor submits a claim under this investment agreement, the investor consents that the host state may submit a counterclaim pursuant to paragraph 2.</p> <p>2. The host state may make a counterclaim:</p> <ul style="list-style-type: none">a) in connection with the factual or legal basis of the claim, andb) that the claimant has breached its obligations under [this investment agreement or international law, domestic laws of the host state or of any third state expressly designated by the parties, or investment contracts]. <p>3. [The selected arbitral tribunal] shall decide any counterclaims on the basis of this investment agreement, the general principles of international law, and, for the avoidance of any doubt, on the basis of any rules of law designated in paragraph (2)(b).</p>

Figure 32: Model Counterclaim Provision

As explained, the Model Provision builds on the model language of Draft Provision D, acknowledging the extensive work of UNCITRAL WG III. Where the language of the Model Provision departs from Draft Provision D, the report provides an explanation as to the reasons underlying the different wording. **Figure 33** below showcases some of the main differences between the Model Provision and Draft Provision D.

Model Counterclaim Provision	UNCITRAL Draft Provision D
<p>1. When an investor submits a claim under this investment agreement, the investor consents that the host state may submit a counterclaim pursuant to paragraph 2.</p> <p>2. The host state may make a counterclaim:</p> <p>a) in connection with <u>the factual or legal basis</u> of the claim, and</p> <p>b) that the claimant has breached its obligations under [this investment agreement or international law, domestic laws of the host state or of any third state expressly designated by the parties, or investment contracts].</p> <p>3. [The selected arbitral tribunal] shall decide any counterclaims on the basis of this investment agreement, the general principles of international law, and, for the avoidance of any doubt, on the basis of any rules of law designated in paragraph (2)(b).</p>	<p>1. The respondent may make a counterclaim:</p> <p>a) arising directly out of <u>the subject matter</u> of the dispute; [or]</p> <p>b) in connection with <u>the factual and legal basis</u> of the claim; or</p> <p>c) that the claimant has breached its obligations under [this or any other applicable treaty, international law, domestic laws or investment contracts].</p> <p>2. For the avoidance of doubt, the consent of the respondent to the submission of a claim by the claimant is subject to the condition that the claimant consents to the submission of counterclaims referred to in paragraph 1.</p>

Figure 33: Comparison between the Model Provision and UNCITRAL Draft Provision D

The Model Counterclaim Provision is also compared to other existing counterclaim provisions incorporated in the investment agreements reviewed in this report (see **Figure 34** below).¹³¹

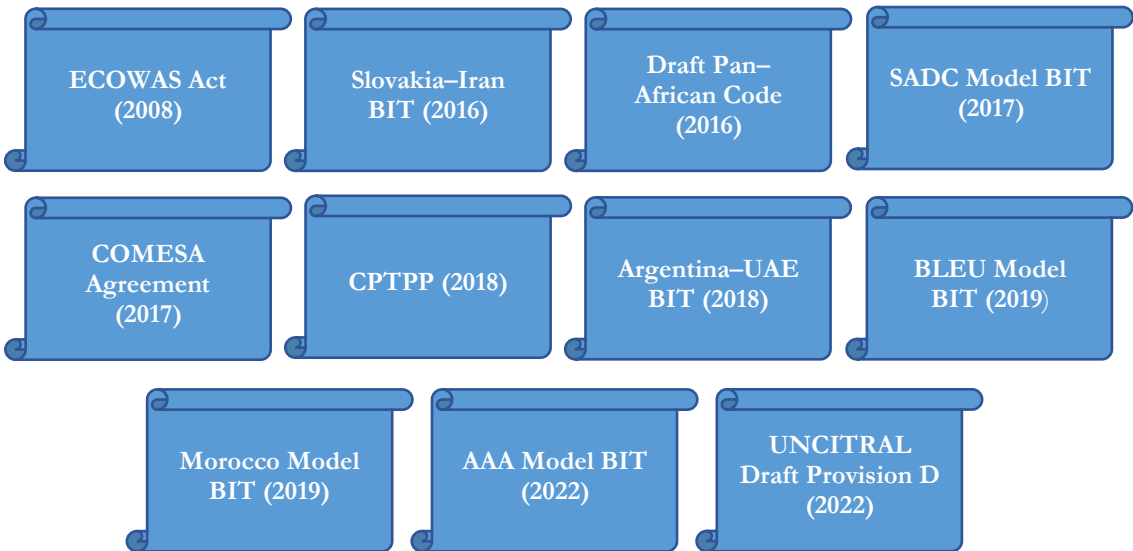


Figure 34: Investment agreements examined in the report

These comparisons show the myriad of linguistic options available to treaty-drafters and illustrate the choices of wording that can be used to achieve host states’ policy goals without compromising on investor protection and regulatory freedom. The report focuses on the practical implications of

¹³¹ The text of these counterclaim provisions is reported in full in **Appendix 1**.

each provision’s linguistic features and shows how the Model Counterclaim Provision either integrates or departs from these features.

5.1 Comparison of the Model Provision With Other Counterclaim Provisions: Jurisdiction and Admissibility

Paragraphs (1) and (2) of the Model Provision stipulate that: *“(1) [w]hen an investor submits a claim under this investment agreement, the investor consents that the host state may submit a counterclaim pursuant to paragraph 2”* and *“(2)[...] [t]he host state may make a counterclaim: (a) in connection with the factual or legal basis of the claim [...]”*. The Model Provision incorporates the express consent of the investor to state counterclaims alongside a broad connection requirement aimed at enabling host states to submit counterclaims more easily. This is aimed at addressing arbitral tribunals’ hesitancy to find implicit consent and a connection between the counterclaim and the primary claim in narrowly worded dispute resolution provisions (*see Section 2.3* outlining the key findings on jurisdiction and admissibility).

Jurisdiction. The Model Provision provides for the investor’s express consent to counterclaims once the investor decides to bring a claim under the investment agreement. The counterclaim provisions codified in the investment agreements reviewed in this report also provide for the investor’s explicit consent to counterclaims in their respective dispute resolution provisions (*see Figure 35* below). This is a novelty featuring in several modern investment agreements whereby host states prefer not to rely on the investor’s implicit consent to counterclaims, as this has often raised questions as to the possibility for the arbitral tribunal to hear the counterclaim.¹³²

Investment Agreements	Jurisdiction
Model Provision	Paragraph (1): When an investor submits a claim under this investment agreement, the investor consents that the host state may submit a counterclaim pursuant to paragraph 2.
Draft Provision D	Paragraph (3): [...] the consent of the respondent to the submission of a claim by the claimant is subject to the condition that the claimant consents to the submission of counterclaims referred to in paragraph 1.

¹³² See Section 2.1.1.

<p style="text-align: center;">Slovakia–Iran BIT (2016)</p>	<p>Article 16(1): Each Contracting Party consents to the submission of a claim of breach of the obligations under Section B to arbitration under this Section in accordance with this Agreement.</p> <p>Article 17(1): The claimant may submit the claim to arbitration if, cumulatively:</p> <p>a) the claimant gives express and written consent:</p> <p>i. to pursue its claim in arbitration under this Article; and</p> <p>ii. that the Host State may pursue any defense, counterclaim, right of set off or other similar claim pursuant to Article 14 of this Agreement in arbitration under this Section; [...].</p> <p>Article 14(3): The respondent may assert as a defense, counterclaim [...].</p>
<p style="text-align: center;">COMESA Agreement (2017)</p>	<p>Article 36(6): Each Member State consents to the submission of a claim to arbitration under this Agreement in accordance with its provisions. Each COMESA investor, by virtue of establishing or continuing to operate or own an investment subject to this Agreement, consents to the terms of the submission of a claim to dispute resolution under this Agreement.</p> <p>Article 36(7): A Member State against whom a claim is brought by a COMESA investor or its investment under this Article, may assert as a defence, counterclaim [...].</p>
<p style="text-align: center;">CPTPP (2018)</p>	<p>Article 9.20(1): Each Party consents to the submission of a claim to arbitration under this Section in accordance with this Agreement.</p> <p>Article 9.21(2): No claim shall be submitted to arbitration under this Section unless:</p> <p>(a) the claimant consents in writing to arbitration in accordance with the procedures set out in this Agreement [...].</p> <p>Article 9.19(2): When the claimant submits a claim pursuant to paragraph 1(a)(i)(B), 1(a)(i)(C), 1(b)(i)(B) or 1(b)(i)(C), the respondent may make a counterclaim [...].</p>
<p style="text-align: center;">Argentina–UAE BIT (2018)</p>	<p>Article 23: Each Party consents to submit a claim to arbitration under this Section in accordance with this Agreement.</p> <p>Article 22(1): [...] the claimant may only submit a claim to arbitration under this Section provided that: (a) the claimant consents to submit to arbitration in accordance with the procedures set forth in this Agreement; [...].</p> <p>Article 28(4): [...] Upon submission of its counter-memorial [...] the respondent may submit a counter-claim [...].</p>
<p style="text-align: center;">EU–Chile AFA (2022)</p>	<p>Article 10.31(1): The respondent consents to the submission of a claim under this Section.</p> <p>Article 10.31(3): The claimant is deemed to give consent in accordance with the procedures provided for in this Section at the time of submitting a claim pursuant to Article 10.29 (Submission of a Claim).</p> <p>Article 10.30(1): The respondent may submit a counterclaim [...].</p> <p>Article 10.30(3): For greater certainty, claimant’s consent to the procedures under this Section includes the submission of counterclaims by the respondent.</p>

Figure 35: Jurisdiction over counterclaims in the Model Provision, UNCITRAL Draft Provision D and the reviewed investment agreements

The COMESA Agreement, the CPTPP and the Argentina/UAE BIT expressly provide that the respondent (*i.e.* the host state) may submit a counterclaim against the claimant (*i.e.* the investor) but they derive the claimant’s consent to the submission of counterclaims from the claimant’s acceptance (for CPTPP in writing) to submit to arbitration in accordance with the procedures set forth in the relevant investment agreement. The EU/Chile AFA goes further by making it explicit that the “claimant’s consent to the procedures [set forth in the investment agreement] includes the submission of counterclaims by the respondent”.

The Slovakia-Iran BIT is the most progressive provision in terms of ensuring the claimant’s consent to state counterclaims by subjecting the claimant’s ability to bring a claim under the agreement to its express and written consent to the submission of counterclaims by the respondent. The Model Provision follows a similar approach, although it does not require the consent of the investor in writing, departing in this respect from the Slovakia/Iran BIT counterclaim provision.

The Model Provision also departs from the complex (and somewhat convoluted) language of UNCITRAL Draft Provision D which, as explained in **Section 4.2** above, follows a “conditional approach”. In fact, Draft Provision D subjects the respondent’s consent to the submission of a claim by the claimant to the condition that the claimant consents to the submission of counterclaims by the respondent. The approach adopted in the Model Provision, besides providing greater legal certainty, also avoids the risk that a claim brought by an investor may be invalidated once arbitration proceedings are ongoing if the investor chooses to withhold consent to state counterclaims at a later stage. Finally, the Model Provision also avoids using the terms “claimant” and “respondent” opting instead for “investor” and “host state” to provide greater clarity.

Figure 36 below summarizes the different approaches concerning the combined consent of host states and investors to the submission of claims and counterclaims.

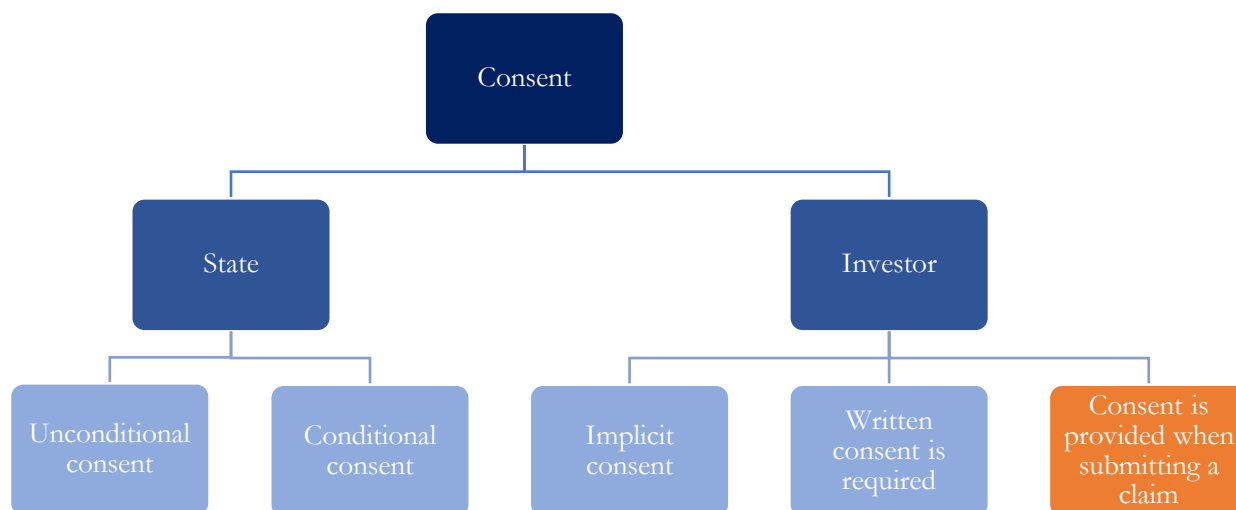


Figure 36: Flow chart summarizing different options for consent to the submission of claims and counterclaims

By expressly stating that the investor consents to the submission of counterclaims when bringing a claim under the investment agreement, the Model Provision thus provides the greatest legal certainty and predictability.

Admissibility. The Model Provision incorporates a broad connection requirement that makes a counterclaim admissible when there is either a legal *or* factual connection between the host state’s counterclaim(s) and the investor’s primary claim(s). The proposed wording broadens the scope of counterclaims that can be proceed to the merits, by establishing that a factual connection (or a legal connection) between the counterclaim and the primary claim is sufficient on its own for a counterclaim to be admissible.

The investment agreements reviewed in this report do not all include an express connection requirement and follow different approaches which can be categorized in three groups: (1) the absence of any reference to a connection requirement;¹³³ (2) a requirement that the counterclaim be “directly related with the dispute” or “aris[e] directly out of the subject matter of the dispute” (*see* **Figure 37** below); (3) a requirement that the counterclaim be “in connection with the factual *and* legal basis of the claim” (*see* **Figure 37** below).

Investment Agreements	Admissibility
Model Provision	Paragraph (2)(a): in connection with the factual or legal basis of the claim [...]

¹³³ This is the approach followed in the SADC Model BIT, the ECOWAS Act, the COMESA Agreement, the Draft Pan–African Code, the Slovakia/Iran BIT, the Morocco Model BIT, the BLEU Model BIT and the AAA Model BIT. *See infra* **Appendix 1**.

Draft Provision D	Paragraph 1: The respondent may make a counterclaim: a) arising directly out of the subject matter of the dispute; [or] b) in connection with the factual and legal basis of the claim ; or [...]
CPTPP (2018)	Article 9.19(2): [...] the respondent may make a counterclaim in connection with the factual and legal basis of the claim [...].
Argentina–UAE BIT (2018)	Article 28(4): [...] the respondent may submit a counter-claim directly related with the dispute [...].
EU-Chile AFA (2022)	Article 10.30(3): The respondent may submit a counterclaim [...] arising in connection with the factual basis of the claim .

Figure 37: Admissibility in the Model Provision, UNCITRAL Draft Provision D and the reviewed investment agreements

(1) *Absence of any reference to a connection requirement.* In the absence of any reference to a connection requirement, arbitral tribunals can exercise great discretion on finding a counterclaim (in)admissible. In these circumstances, tribunals are free to determine whether a connection between the counterclaim and the primary claim is required and, most importantly, what kind of connection is required (factual or legal or both), which, in turn, may generate legal uncertainty. Tribunals can, however, be constrained to find such a connection by the applicable Arbitration Rules, such as, for example, Rule 48 of the ICSID Arbitration Rules.¹³⁴ But even when the relevant arbitration rules are silent on this point (*e.g.* Article 21(3) of the revised UNCITRAL Arbitration Rules),¹³⁵ tribunals tend to look for at least some form of connection between the counterclaim and the primary claim before allowing the counterclaim to proceed to the merits^{136, 137}. Hence, this option offers parties the least legal certainty.

(2) *A requirement that the counterclaim be “directly related with the dispute” or “aris[e] directly out of the subject-matter of the dispute”.* The language “directly related with the dispute” (*see* Argentina/UAE BIT) or “arising directly out of the subject-matter of the dispute” (*see* Draft Provision D) does not clarify whether the connection between the host state’s counterclaim(s) and the investor’s claim(s) should be either legal or factual or both. This language leaves it up to the arbitral tribunal to decide whether a factual or legal (or both factual and legal) connection between the counterclaim and the

¹³⁴ *See* Section 2.1.2 above.

¹³⁵ *See* Section 2.2.2 above.

¹³⁶ In this sense, even if Draft Provision D gives host states the option not to include any admissibility requirement in their counterclaim provision (*see* conjunction “or” in between paragraphs 1(a), 1(b) and 1(c) in **Figure 37**), it is likely than an arbitral tribunal would look for some type of connection between the counterclaim and the primary claim before declaring that the counterclaim can be heard.

¹³⁷ *See* Section 2.3 above.

primary claim is required. Depending on the tribunal’s interpretation, it may be easier (e.g. if the tribunal considers a factual connection sufficient) or harder (e.g. if the tribunals requires a strict legal connection) for a counterclaim to be considered admissible.¹³⁸ This approach however creates legal uncertainty.

(3) A requirement that the counterclaim be “in connection with the factual and legal basis of the claim”. The wording “in connection with the factual *and* legal basis of the claim” (see CPTPP and Draft Provision D) imposes a higher threshold than the wording “in connection with the factual *or* legal basis of the claim” (see Model Provision). The conjunction “and” indicates that the connection between the state counterclaim(s) and the investor’s primary claim(s) must both legal and factual. This approach makes it harder for an arbitral tribunal to consider admissible a counterclaim that is not based on a violation arising from the same legal instrument invoked by the claimant. This is showcased in **Figure 38** below.

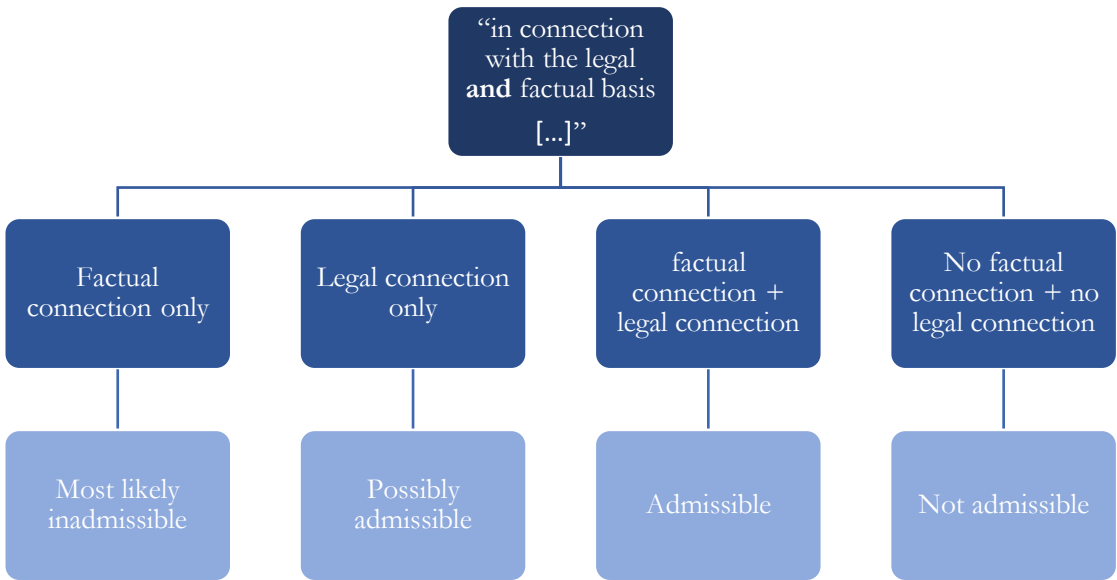


Figure 38: Decision map showcasing the consequences of a counterclaim provision requiring a factual “and” a legal connection (see CPTPP and Draft Provision D)

In the same vein, the use of the conjunction “and” constrains arbitral tribunals’ discretion in finding a counterclaim admissible on the sole basis of a factual connection, which is the trend that tribunals seem to be following in recent cases.¹³⁹ The EU/Chile AFA endorses this trend by stipulating that a sole connection with “the factual basis of the claim” is sufficient to make a counterclaim admissible.

¹³⁸ See **Section 2.3** above.

¹³⁹ See e.g. *Urbaser v. Argentina* (n 28), para. 1151: “The Tribunal observes that the factual link between the two claims is manifest [...]. This would be sufficient to adopt jurisdiction over the Counter-claim as well.”

Building on option (2), the Model Provision opts for a broad connection requirement allowing for a counterclaim to be admissible when there is either a factual “or” legal connection between the counterclaim and the primary claim. This is showcased in **Figure 39** below.

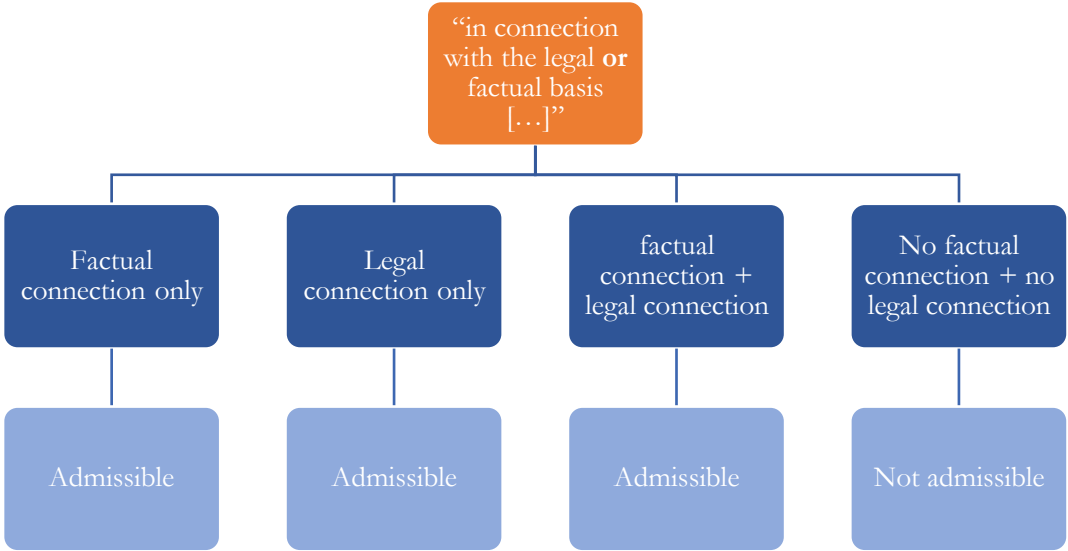


Figure 39: Decision map showcasing the consequences of a counterclaim provision requiring a factual “or” a legal connection (see Model Counterclaim Provision)

Figure 40 below summarizes the impact that the wording concerning the connection between a state counterclaim and the investor’s primary claim may have on the admissibility of a counterclaim.

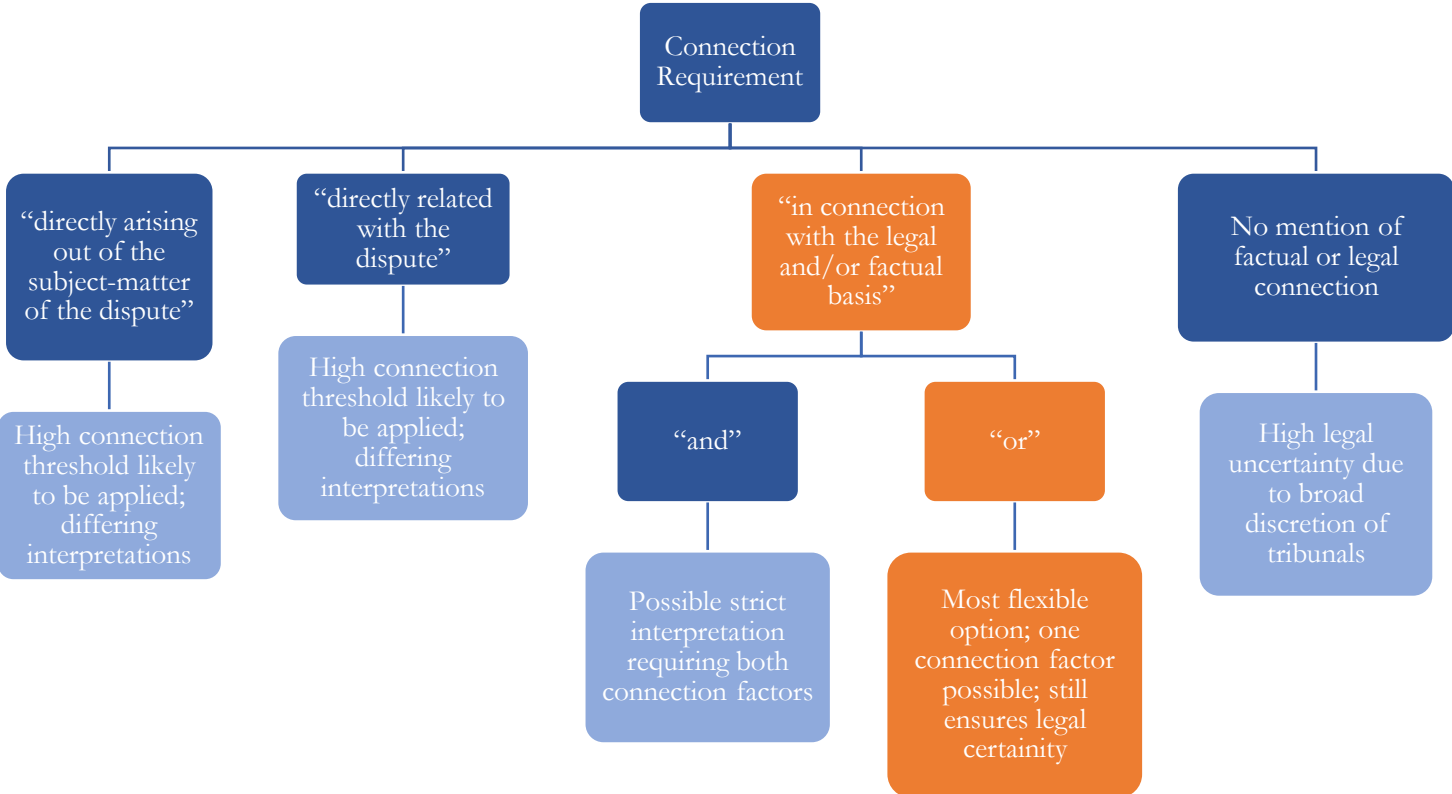


Figure 40: Possible wording concerning the admissibility of counterclaims

Figure 40 also showcases that the Model Provision (highlighted in orange) proposes the most flexible approach. Treaty-drafters can however opt for a higher admissibility threshold by using the conjunction “and” to require a stricter connection between the counterclaim and the primary claim (*see Figure 38* above).

5.2 Comparison of the Model Provision With Other Counterclaim Provisions: Applicable Law and Investor Obligations

When it comes to counterclaims, applicable law and investor obligations form a symbiotic relationship. The cause-of-action for a counterclaim can be found either in direct investor obligations stipulated in the investment agreement and/or, indirectly, in the bodies of law applicable to the merits of the dispute. While direct investor obligations are crucial to making state counterclaims more likely to succeed on the merits, they are also a contentious topic of discussion in treaty negotiations and, so far, have only featured in some modern investment agreements. For this reason, the possibility of sourcing investor obligations indirectly from the law applicable to the merits of the dispute is an alternative that deserves consideration, especially in light of the recent findings on this point in *Aven v. Costa Rica* and *Urbaser v. Argentina*.

Host states concerned with predictable legal outcomes should carefully consider the scope of the law chosen to apply to the merits, as this is the law that the arbitral tribunal will interpret and apply to their counterclaims. At the same time, they should also be mindful that limiting the scope of the law applicable to the merits is a double-edged sword, as a limitation to the scope of the applicable law may also translate, indirectly, into a limitation as to the sources from which investor obligations can be imported.

The Model Provision makes the relationship between applicable law and investor obligations explicit. It stipulates that:

1. The respondent may make a counterclaim:

[...]

(2)(b) that the claimant has breached its obligations under [this investment agreement or international law, domestic laws of the host state or of any third state expressly designated by the parties, or investment contracts].

(3) [The selected arbitral tribunal] shall decide any counterclaims on the basis of this investment agreement, the general principles of international law, and, for the avoidance of any doubt, on the basis of any rules of law designated in paragraph (2)(b).

Paragraph 2(b) covers the bodies of law from which investor obligations can be sourced, while paragraph 3 covers the law applicable to the merits of the counterclaim. Paragraph 3 identifies (a) the investment agreement, (b) the general principles of international law and (c) any other body of law designated in paragraph 2(b) (*i.e.* domestic laws of the host state or of any other third state, or investment contracts) as the law applicable to the merits of the counterclaim. This cross-reference creates coherence between the law from which investor obligations can be sourced and the law applicable to the merits of the counterclaim. This careful consideration of the inherent relationship between investor obligations and applicable law, and the recommendation that parties explicitly designate the law applicable to counterclaims, is a reaction to tribunals' often unpredictable approach to choice-of-law analysis.

The flexibility provided in paragraph 3 also addresses the concern expressed by some host states that tribunals may interpret their counterclaims in light of bodies of law outside the scope of the parties' intentions. In this sense, the proposed approach allows room for adjustments and strategic choices by treaty negotiators who may be willing to include or exclude bodies of law such as domestic law.

Applicable Law. When compared to Draft Provision D and the counterclaims provisions incorporated in the investment agreements reviewed in the report, it becomes apparent that the suggested Model Provision adopts a novel approach. In fact, the Model Provision is the only counterclaim provision that provides for a **counterclaim-specific choice of law** (which, in turn, mirrors the law from which investor obligations can be sourced) (*see* **Figure 41** below). Draft Provision D does not include any counterclaim-specific choice of law (*see* **Figure 41** below). From this follows that, in an investment agreement incorporating a counterclaim provision modelled on Draft Provision D, the law applicable to a counterclaim would need to be inferred from the general applicable law provision codified in the investment agreement (provided that such provision exists).

Similarly, none of the investment agreements reviewed in the report incorporate a counterclaim-specific choice of law (*see* **Figure 41** below). Some of the treaties reviewed do not contain a general

applicable law provision,¹⁴⁰ while others contain an applicable law provision that refers exclusively to claims.¹⁴¹ Other treaties again contain a general applicable law provision covering “disputes” arising under the investment agreement, which can be understood to refer both to claims and counterclaims. The language used is “a dispute in accordance with this Agreement” (*see* Article 30(1) of the Argentina/UAE BIT), “issues in dispute” (*see* Article 19(1) of the Slovakia/Iran BIT and Article 9.25(1) of the CPTPP), “any [claim or] dispute arising from this Code” (*see* Article 44 of the Draft PAIC), or “a dispute filed with an arbitral tribunal” (*see* Article 41(1) of the Morocco Model BIT).¹⁴²

Investment Agreements	Applicable Law Provision
Model Provision	<p>Paragraph (2): The host state may make <u>a counterclaim</u>: [...] (b) that the claimant has breached its obligations under [this investment agreement or international law, domestic laws of the host state or of any third state expressly designated by the parties, or investment contracts].</p> <p>Paragraph (3): [The selected arbitral tribunal] shall decide <u>any counterclaims</u> on the basis of this investment agreement, the general principles of international law, and, for the avoidance of any doubt, on the basis of any rules of law designated in paragraph (2)(b).</p>
Draft Provision D	No applicable law provision.
Slovakia–Iran BIT (2016)	<p>Article 19(1): A tribunal established under this Section shall decide the <u>issues in dispute</u> in accordance with:</p> <p>a) this Agreement; and b) applicable rules of international law.</p>
Draft Pan–African Code (2016)	<p>Article 44: <u>Any claim or dispute arising from this Code</u> shall be decided in accordance with the provisions of this Code as well as any other national, regional or international laws, rules or principles.</p>
SADC Model BIT (2017)	<p>Article 31(1): When <u>a claim</u> is submitted to a tribunal under this Agreement, it shall be decided in accordance with this Agreement. The governing law for the interpretation of this Agreement shall be this Agreement and the general principles of international law relating to the interpretation of treaties, including the presumption of consistency between international treaties to which the State</p>

¹⁴⁰ These are the 2017 COMESA Agreement and the 2022 AAA Model BIT.

¹⁴¹ *See e.g.* ECOWAS Act, Article 36: “When a claim is submitted to a panel or an appeal tribunal, it shall be decided in accordance with this Supplementary Act, and subsidiarily, any other national, Community, and international law/rules agreed upon by the parties”.

¹⁴² Albeit using a different language, the 2019 BLEU Model BIT also contains a general applicable law provision which can be understood to cover both claims and counterclaims. Article I provides: “A Tribunal established under this Chapter shall render its decision consistent with this Agreement as interpreted in accordance with the Vienna Convention on the Law of Treaties, and other rules and principles of international law applicable between the Contracting Parties” (emphasis added).

	<p>Parties are party. For matters related to domestic law, the national law of the Host State shall be resorted to as the governing law.</p> <p>Article 31(2): For greater certainty, paragraph 31(1) does not expand or alter the scope of obligations contained in this Agreement or incorporate other standards except where specifically expressed herein.</p>
CPTPP (2018)	<p>Article 9.25(1): Subject to paragraph 3, when <u>a claim</u> is submitted under Article 9.19.1(a)(i)(A) (Submission of a Claim to Arbitration) or Article 9.19.1(b)(i)(A), the tribunal shall decide the <u>issues in dispute</u> in accordance with this Agreement and applicable rules of international law.</p>
Argentina–UAE BIT (2018)	<p>Article 30(1): The Arbitral Tribunal shall decide <u>a dispute in accordance with this Agreement</u>, and shall apply the law of the State Party to the dispute (including its rules on the conflict of laws) and such rules of international law as may be applicable.</p>
Morocco Model BIT (2019)	<p>Article 41(1): <u>A dispute</u> filed with an arbitral tribunal shall be decided in accordance with the provisions of this Agreement, the national law of the Host Party and the applicable rules of international law.</p>
EU–Chile AFA (2022)	<p>Article 10.24(2): Where applicable, this Section [Resolution of Investment Disputes and Investment Court System] shall also apply to counterclaims in accordance with article 10.30 (Counterclaim).</p> <p>Article 10.37(1): The Tribunal shall determine whether the measure in respect of which <u>the claimant</u> is submitting <u>a claim</u> is inconsistent with any of the provisions [...]</p> <p>Article 10.37(2): In making such determination, the Tribunal shall apply the provisions of this Agreement and other rules of international law applicable between the Parties. It shall interpret this Agreement in accordance with customary rules of interpretation of public international law, as codified in the Vienna Convention on the Law of Treaties.</p> <p>Article 10.37(3): For greater certainty, in determining the consistency of a measure with the provisions referred to in Article 10.24 (1) (Scope and Definitions), the Tribunal shall consider, when relevant, the domestic law of a Party as a matter of fact. In doing so, the Tribunal shall follow the prevailing interpretation given to the domestic law by the courts or authorities of that Party and any meaning given to domestic law by the Tribunal shall not be binding upon the courts or authorities of that Party.</p>

Figure 41: Law applicable to counterclaims in the Model Provision, UNCITRAL Draft Provision D and the reviewed investment agreements

The SADC Model BIT also contains an applicable law provision which, as such, does not cover counterclaims, as it refers exclusively to “a claim [...] submitted to a tribunal under this Agreement” (see Article 31.1 of SADC Model BIT in **Figure 41** above). However, the same provision refers to the “governing law for the interpretation of this Agreement”, which in turn can be understood to refer to the Agreement as a whole (including the counterclaim provision stipulated at Article 19.2).

Finally, the EU/Chile AFA adopts the most progressive approach. In fact, while Articles 10.37(1) and 10.37(2) set out the bodies of law that a tribunal is asked to apply when deciding over a claim brought forward by the investor, these same rules can be understood to apply to counterclaims submitted by the relevant host state (*see* **Figure 41** above). This interpretation can be inferred from Article 10.24(2) which states that Section D of the Chile/EU AFA, entitled Resolution of Investment Disputes and Investment Court System, “shall also apply to counterclaims in accordance with article 10.30 (Counterclaim)”. The EU/Chile AFA thus stands out as the only investment agreement of those reviewed in the report that, albeit via a cross-reference, provides for a choice of law that, although designed to cover claims only, can also be extended to counterclaims.

The Model provision, with its proposed counterclaim-specific choice of law, goes even further. First, it gives host states the choice to select the bodies of law that should be applied to their counterclaims. Second, it gives host states the possibility to select different bodies of law for application to investors claims, on the one hand, and to their counterclaims, on the other. In short, the approach proposed by the Model Provision provides greater flexibility and legal certainty than any of the other approaches examined in this report. Such an approach becomes of even greater importance for investment agreements that do not have a general applicable law provision.

Investor Obligations. Building on Draft Provision D, which refers to several bodies of law which can be used to source investor obligations, paragraph 2(b) of the Model Provision also lists several sources for this purpose: these are (a) the investment agreement itself,¹⁴³ (b) international law, (c) the domestic law of the host state, (d) the domestic law of any third state expressly designated by the parties, and (e) investments contracts (*see* **Figure 42** below). The enumerated list of sources is presented in brackets to give parties ultimate discretion as to what bodies of law to include/exclude. This flexibility is further confirmed by the use of the conjunction “or” between the different bodies of law listed.

Both the Model Provisions and Draft Provision D do not, on their own, establish direct investor obligations (*e.g.* obligation to comply with domestic laws). As pointed out by the UNCITRAL WG III in its ISDS project of reform, such obligations are, however, of fundamental importance in the context of counterclaims raised in treaty-based investment disputes. On this point, the WG stated:

¹⁴³ Draft Provision D also adds “any other applicable treaty”, which may be understood to cover treaties to which both parties are signatories.

Yet, in order to raise counterclaims in treaty-based investment disputes, the substantive obligations, the breach of which would form the basis of the counterclaims, would need to be included in the respective treaty.¹⁴⁴

While older investment agreements do not contain direct investor obligations, these obligations have become increasingly common in modern investment agreements, such as those reviewed in the report. A complete list of the investor obligations codified in the reviewed treaties is provided in **Appendix 2**. These obligations range from hard obligations (the modal verb used is “shall”) to soft or best-efforts obligations (the modal verb used is “should”). Article 22 of the Draft PAIC is an example of a hard investor obligation. It provides:

Article 22
Corporate Social Responsibility

1. Investors **shall abide** by the laws, regulations, administrative guidelines and policies of the host State.
2. Investors **shall**, in pursuit of their economic objectives, **ensure** that they do not conflict with the social and economic development objectives of host States and shall be sensitive to such objectives.
3. Investors **shall contribute** to the economic, social and environmental progress with a view to achieving sustainable development of the host State.

Article 10(3) of the Slovakia-Iran BIT is an example of a soft or best-efforts investor obligation. It stipulates:

ARTICLE 10
Environmental and labor rights and other standards

[...]

3. Investors and investments **should apply** national, and internationally accepted, standards of corporate governance for the sector involved, in particular for transparency and accounting practices. Investors and their investments **should strive to make** the maximum feasible contributions to the sustainable development of the Host State and local community through appropriate levels of socially responsible practices.

The distinction between hard and soft investor obligations is not without significance. It is, in principle, easier to source counterclaims from hard obligations rather than soft or best-efforts obligations, as it is unclear whether these softer obligations are legally binding. Despite this observation, it should also be noted that even these softer obligations must carry (some) legal weight, or else there would not have been much point in including them in an investment agreement. For example, such obligations could be used for interpretive purposes (*e.g.* to determine

¹⁴⁴ UNCITRAL WG III (Investor-State Dispute Settlement Reform) (n 118), para. 50.

the investor’s good faith and overall conduct) by an arbitral tribunal when deciding over a state counterclaim.

Most of the treaties reviewed in this report do not mention specific investor obligations in the counterclaim provision itself, but rather in separate provisions of the agreement. The CPTPP, the Argentina/UAE BIT and the BLEU Model BIT, for example, all provide for direct investor obligations (*e.g.* on corporate social responsibility) (*see* **Appendix 2**); their counterclaim provisions, however, do not establish a direct connection between the submission of a counterclaim and a “breach” of an obligation codified in the agreement or of the agreement itself (*see* **Appendix 1**). While this choice might create uncertainty as to the obligations that can form the basis of a counterclaim, it can also provide flexibility by not limiting the scope of the obligations on which a state can base its counterclaim to those codified in the agreement.

The SADC Model BIT follows a different approach. Like the CPTPP, the Argentina/UAE and the BLEU Model BIT, it codifies direct investor obligations in separate provisions of the agreement (*see* **Appendix 2**). However, unlike these agreements, it makes the connection between the counterclaim and a “breach” of the agreement explicit in the counterclaim provision. Article 19(2) provides:

A Host State may initiate **a counterclaim** [...] for damages or other relief **resulting from an alleged breach of the Agreement**.

The ECOWAS Supplementary Act, the Draft PAIC, the COMESA Agreement, and the AAA Model BIT follow a similar approach (*see* **Figure 45** below). Unlike the CPTPP, the Argentina/UAE and the BLEU Model BIT, however, these treaties do seem to limit the scope of the obligations which can form the basis of a counterclaim to those codified in the investment agreement itself.

Investment Agreements	Counterclaim Provisions and Investor Obligations
Model Provision	Paragraph (2): The host state may make a counterclaim: [...] (b) that the claimant has breached its obligations under [this investment agreement or international law, domestic laws of the host state or of any third state expressly designated by the parties, or investment contracts]. ”
Draft Provision D	Paragraph 1(c): The respondent may make a counterclaim [...] “that the claimant has breached its obligations under [this or any other applicable treaty, international law, domestic laws or investment contracts]. ”

ECOWAS Act (2008)	Article 18(5): A host Member State may initiate a counterclaim [...] for damages resulting from an alleged breach of the Supplementary Act .
Draft Pan–African Code (2016)	Article 43(2): A Member State may initiate a counterclaim [...] for damages or other relief resulting from an alleged breach of the Code .
COMESA Agreement (2017)	Article 36(7): A Members State against whom a claim is brought by a COMESA investor [...] may assert as a [...] counterclaim [...] that the COMESA investor or its investment bringing the claim has not fulfilled its obligations under this Agreement, including the obligations to comply with all applicable domestic measures [...].
Morocco Model BIT (2019)	Article 28(4): Where an investor or its investment has failed to comply with its obligations under Article 18 (Compliance with Domestic Laws and International Obligations) or has violated Article 19 (Anti-Corruption, Anti-Money Laundering and Anti-Terrorist Financing), the Host Party may file a counterclaim in any court established pursuant to this Section.
AAA Model BIT (2022)	Article 22(G)(1): A Respondent may initiate a Counterclaim for breach of the obligations set out under this Agreement [...]
EU–Chile AFA (2022)	Article 10.30(1): The respondent may submit a counterclaim on the basis of an investor’s failure to comply with an international obligation applicable in the territories of both Parties, ²⁶ [...] ²⁷ ²⁶ For greater certainty, the obligations referred to in this paragraph shall be based on legal commitments that the Parties have consented to . ²⁷ The Joint Council/Committee shall, at the request of a Party, issue binding interpretations pursuant to article [insert] to clarify the scope of international obligations that are referred to in this paragraph.

Figure 42: Counterclaims Provisions and Investor Obligations in the Model Provision, UNCITRAL Draft Provision D and the reviewed investment agreements

The Slovakia/Iran BIT and the Morocco Model BIT follow an even stricter approach and refer directly to substantive investor obligations in the same counterclaim provisions. Article 14(3) of the Slovakia-Iran BIT provides that:

“[t]he respondent may assert as a [...] counterclaim [...] that the claimant has **not fulfilled its obligations under this Agreement to comply with the Host State law**”.

This wording limits the scope of the obligations on which the host state can base a counterclaim to obligations of the investor to comply with the host state’s domestic law. The wording also indicates that a breach of the relevant host state law can form the basis of a counterclaim to the extent that such breach also constitutes a breach of the investment agreement.

The Morocco Model BIT goes further and includes the relevant investor obligations in the text of the counterclaim provision by cross-referring to the relevant articles in the treaty (*i.e.* Article 18 on Compliance with Domestic Laws and International Obligations and Article 19 on Anti-Corruption, Anti-Money Laundering and Anti-Terrorist Financing) (*see* **Figure 42** above). It should also be noted that the counterclaim provision in the Morocco Model BIT does not mention or cross-refer to Article 20 of the agreement, which covers investors' best-efforts obligations on social and environmental responsibility. From this follows that, under the Morocco Model BIT, not all breaches of investor obligations can give rise to counterclaims: while a host state could base a counterclaim on a breach of the obligations set out at Articles 18 and 19, it would, in principle, not be possible for it to base a counterclaim on a breach of the obligations set out at Article 20. This interpretation would be consistent with the choice of the parties to include only hard obligations in the counterclaim provision. The situation would, however, be different if the treaty contained both hard and soft investor obligations but did not refer to any obligations in its counterclaim provision. In fact, in this latter case, given the absence of an express reference to any investor obligations in the counterclaim provision, it would (arguably) be easier to base a counterclaim, at least in part, even on a soft obligation.

Finally, the EU/Chile AFA adopts a yet different approach. The agreement stands out as it does not contain any specific investor obligations in its text. The counterclaim provision at Article 10.30 refers generally to a counterclaim based on "an investor's failure to comply with an international obligation applicable in the territories of both Parties", thus incorporating by reference international investor obligations outside the four-corners of the agreement (*see* **Figure 42** above). The reference to "international obligations" makes it clear that domestic or contractual investor obligations that cannot be elevated to the international plane are excluded from the scope of application of the counterclaim provision. This choice might be explained by the desire of the parties to avoid arbitral tribunals from interpreting their domestic laws and investment contracts.

Article 10.30 further clarifies, in a footnote, that these obligations must be based "on legal commitments that the Parties have consented to".¹⁴⁵ While this approach might give rise to legal uncertainty, as there is no guidance as to what international obligations are imposed upon investors and can be invoked as the basis of a counterclaim, it is also a highly flexible approach. In fact, it expands the scope of the obligations upon which the host states can (potentially) base their counterclaims (with the caveat mentioned above that pure domestic and contractual obligations

¹⁴⁵ *See* EU/Chile AFA, footnote 26, also reported in **Figure 42** above.

are excluded). It also makes it easier for the agreement to stand the passing of time, as this would not need to be amended on an ongoing basis to incorporate novel investor obligations.

Article 10.30 of the EU/Chile AFA also carves out (in another footnote) the possibility for host states to clarify the scope of investor obligations via a binding joint interpretation issued by the relevant committee established for this purpose.¹⁴⁶ At the time of signature of the investment agreement, Chile, the EU and its Member States issued a joint declaration which, while not focusing on investor obligations, referred to the climate change commitments of the parties under the Paris Agreement.¹⁴⁷ It is thus possible that, if a dispute arose under the agreement and one of the host states were to submit a counterclaim for an investor's breach of an obligation based on these climate change commitments, the arbitral tribunal would have to consider these commitments as capable of giving rise to an investor obligation covered by the agreement.

While flexible, the approach adopted in Article 30.10 of the EU/Chile AFA leaves domestic and contractual investor obligations outside of its scope of application. This counterclaim provision further limits the scope of the counterclaims that can be raised by establishing that the investor obligation on which a counterclaim may be based must be an obligation recognized in both host states involved in the dispute. The Model Provision departs from this approach and, building on Draft Provision D and other relevant counterclaim provisions reviewed in the report, provides treaty drafters with a balanced approach ensuring legal certainty while, at the same time, emphasizing host states' autonomy concerning the law applicable to counterclaims and from which investor obligations can be sourced. to determine what bodies of law can be included in/excluded from the counterclaim-specific applicable law sub-clause and the sub-clause referring to a breach of investor obligations on which the counterclaim can be based.

5.3 Conclusion

Figure 43 illustrates different outcomes of the flexible drafting approach available to treaty-drafters under the Model Provision and offers an interpretive framework for tribunals considering counterclaims brought under such a provision.

¹⁴⁶ See EU/Chile AFA, footnote 27, also reported in **Figure 42** above.

¹⁴⁷ See Joint Interpretative Declaration on the Investment Protection Agreement between Chile and the European Union and its Member States at https://www.eeas.europa.eu/delegations/chile/eu-chile-advanced-framework-agreement_en accessed January 2023.

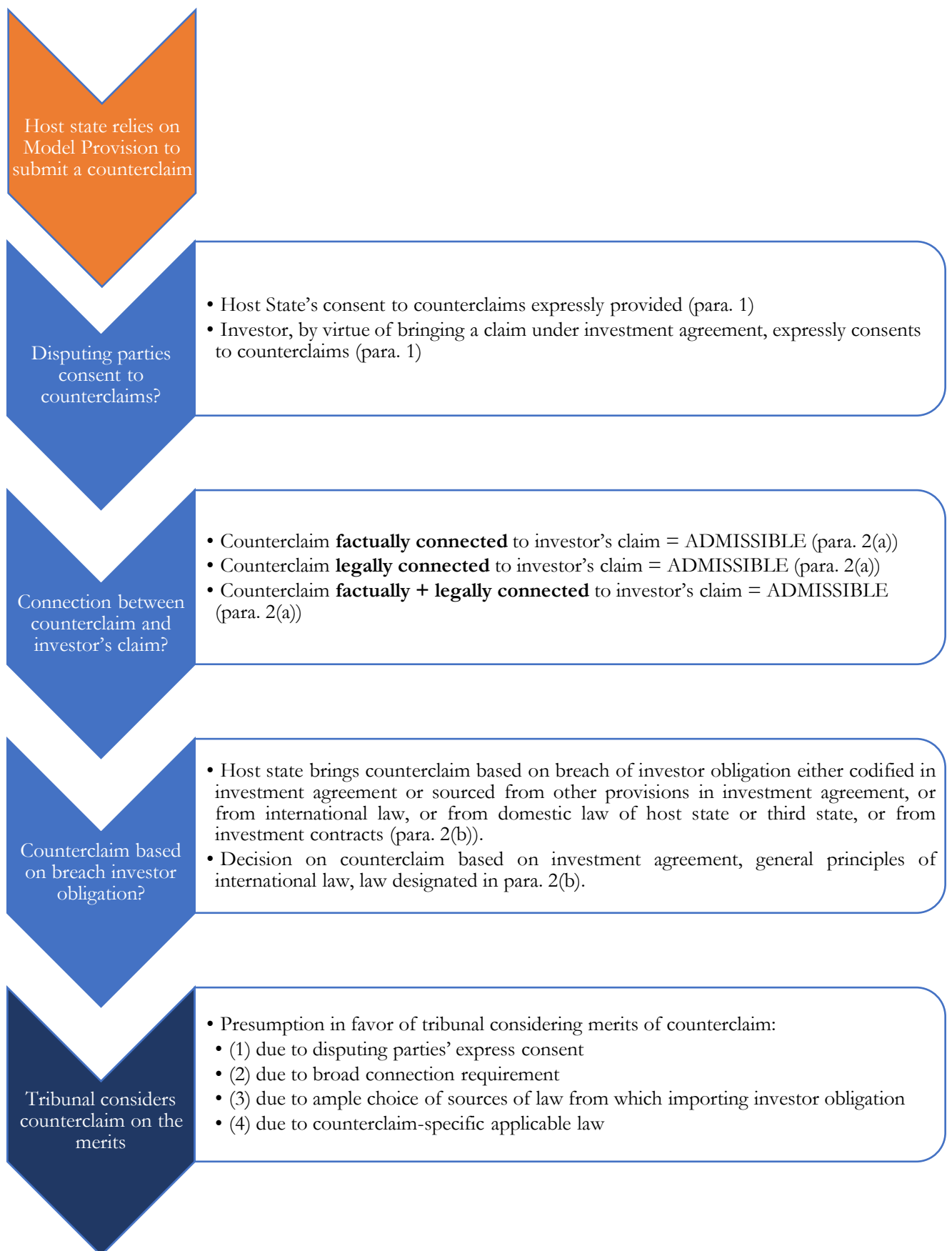


Figure 43: Flowchart showcasing Model Counterclaim Provision

6 Concluding Remarks

This report concludes that counterclaims are a tool available to host states to rebalance the inherent asymmetry of ISDS’ one-way system. However, counterclaim provisions in investment agreements – which enable states to bring counterclaims – only function as intended when carefully drafted. Close attention must be paid to establishing investors’ consent, to connecting the counterclaim with the investors’ claims, and to choosing the law applicable to the counterclaim. The existence of investor obligations in the investment agreement, or alternatively, the ability to source investor obligations from the applicable law chosen by the parties, is also a crucial factor for the success of a counterclaim. The report proposes a model counterclaim provision taking into account all of these factors.

Section 2 analyzed the procedural requirements for bringing a counterclaim under the ICSID Convention, the ICSID Arbitration Rules, and the UNCITRAL Arbitration Rules. Specifically, it identified the major jurisdiction and admissibility hurdles emerging from caselaw which prevent a counterclaim from proceeding to the merits. While considering the relevant jurisprudence of arbitral tribunals, Section 3 identified the impact of the law designated by the parties in the investment agreement on state counterclaims. Also, Section 3 evaluated whether investor obligations – when not codified in the investment agreement itself – can be sourced from other provisions in the investment agreement or from contracts related to the investment, domestic laws, and international law. Section 4 analyzed the counterclaim provision drafted by UNCITRAL WG III and identified its pros and cons. Finally, Section 5 built on the preceding analyses to propose a Model Counterclaim Provision (reported below):

Model Counterclaim Provision
<p>1. When an investor submits a claim under this investment agreement, the investor consents that the host state may submit a counterclaim pursuant to paragraph 2.</p> <p>2. The host state may make a counterclaim:</p> <ul style="list-style-type: none"> a) in connection with the factual or legal basis of the claim, and b) that the claimant has breached its obligations under [this investment agreement or international law, domestic laws of the host state or of any third state expressly designated by the parties, or investment contracts]. <p>3. [The selected arbitral tribunal] shall decide any counterclaims on the basis of this investment agreement, the general principles of international law, and, for the avoidance of any doubt, on the basis of any rules of law designated in paragraph (2)(b).</p>

Figure 44: Model Counterclaim Provision

Building on UNCITRAL Draft Provision D and other existing counterclaim clauses, this Model Provision provides parties with sufficient flexibility as well as a high degree of legal certainty by ensuring investors' consent to counterclaims at the inception of an investment dispute and by broadening the scope of connection that a counterclaim may have to the investor's primary claim. Moreover, the Model Provision proposes a novel approach by including a counterclaim-specific choice-of-law sub-clause and clearly identifying the law from which investor obligations can be sourced.

Appendix 1: Investment Agreements Containing Counterclaim Provisions¹⁴⁸

ECOWAS Act (2008)	Slovakia–Iran BIT (2016)	Draft Pan–African Code (2016)
<p>Article 18(5)</p> <p>A host Member State may initiate a counterclaim before any tribunal established pursuant to this Supplementary Act for damages resulting from an alleged breach of the Supplementary Act.</p>	<p>Article 14(3) General provisions</p> <p>The respondent may assert as a defense, counterclaim, right of set off or other similar claim that the claimant has not fulfilled its obligations under this Agreement to comply with the Host State law or that it has not taken all reasonable steps to mitigate possible damages. For avoidance of any doubt, if the tribunal does not dismiss the claim under paragraph 2¹⁴⁹ above, it shall take such violations into account when assessing the claim if raised as a defense, counterclaim, right of set off or other similar claim by the respondent.</p> <p>Article 17(1) Submission of a Claim to Arbitration</p> <p>1. The claimant may submit the claim to arbitration if, cumulatively:</p> <p>a) the claimant gives express and written consent:</p> <p>i. to pursue its claim in arbitration under this Article; and</p> <p>ii. that the Host State may pursue any defense, counterclaim, right of set off or other similar claim pursuant to Article 14 of this Agreement in arbitration under this Section; [...]</p>	<p>Article 43(3)</p> <p>A Member State may initiate a counterclaim against the investor before any competent body dealing with a dispute under this Code for damages or other relief resulting from an alleged breach of the Code.</p>
SADC Model BIT (2017)	COMESA Agreement (2017)	CPTPP (2018)
<p>Article 19(2)</p> <p>A Host State may initiate a counterclaim against the Investor before any tribunal established pursuant to this Agreement for damages or other relief resulting from an alleged breach of the Agreement.</p>	<p>Article 36(7)</p> <p>A Member State against whom a claim is brought by a COMESA investor or its investment under this Article, may assert as a defence, counterclaim, right of set off or other similar claim, that the COMESA investor or its investment 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.</p>	<p>Article 9.19(2) Submission of a Claim to Arbitration</p> <p>When the claimant submits a claim pursuant to paragraph 1(a)(i)(B), 1(a)(i)(C), 1(b)(i)(B) or 1(b)(i)(C), the respondent may make a counterclaim in connection with the factual and legal basis of the claim or rely on a claim for the purpose of a set off against the claimant.</p>

¹⁴⁸ Colored text key: Procedure = Purple; Consent = Green; Applicable law = Light blue; Parties who can bring a counterclaim = Brown; Type of counterclaim covered = Red; Remedies and defenses = Navy; Unclean hands = Orange; Connection requirement = Pink.

¹⁴⁹ Article 14(2) For avoidance of doubt, an investor may not submit a claim under this Agreement where the investor or the investment has violated the Host State law. The Tribunal shall dismiss such claim if such violation is sufficiently serious or material. For avoidance of any doubt, the following violations shall always be considered sufficiently serious or material to require dismissal of the claim: a) Fraud; b) Tax evasion; c) Corruption and bribery; or d) Investment has been made through fraudulent misrepresentation, concealment, corruption, or conduct amounting to an abuse of process.

Argentina–UAE BIT (2018)	BLEU Model BIT (2019)	UNCITRAL Draft Provision D (2022)
<p>Article 28(4)</p> <p>[...] Upon submission of its counter-memorial, or at a later stage of the proceedings, if the Arbitral Tribunal decides that, under the circumstances, the delay is justified, the respondent may submit a counter-claim directly related with the dispute, provided that the disputing party shall specify precisely the basis for the counter-claim.</p>	<p>Article 19.D(2)</p> <p>2. The claimant may submit the claim to arbitration if, cumulatively:</p> <ol style="list-style-type: none"> a. the claimant gives express and written consent: <ol style="list-style-type: none"> i. to pursue its claim in arbitration under this Article; and ii. that the Host State may pursue any defense, counterclaim, right of set off or other similar claim pursuant to Article 19 of this Agreement in arbitration under this Section; [...] 	<ol style="list-style-type: none"> 1. The respondent may make a counterclaim: <ol style="list-style-type: none"> a. arising directly out of the subject matter of the dispute; [or] b. in connection with the factual and legal basis of the claim; or c. that the claimant has breached its obligations under [this or any other applicable treaty, international law, domestic laws or investment contracts]. 2. For the avoidance of doubt, the consent of the respondent to the submission of a claim by the claimant is subject to the condition that the claimant consents to the submission of counterclaims referred to in paragraph 1.
Morocco Model BIT (2019)	AAA Model BIT (2022)	EU–Chile AFA (2022)
<p>Article 28(4)¹⁵⁰</p> <p>Where an investor or its investment has failed to comply with its obligations under Article 18 (Compliance with Domestic Laws and International Obligations) or has violated Article 19 (Anti-Corruption, Anti-Money Laundering and Anti-Terrorist Financing), the Host Party may file a counterclaim in any court established pursuant to this Section.</p>	<p>G. Counterclaim</p> <ol style="list-style-type: none"> 1. A Respondent may initiate a Counterclaim for breach of the obligations set out under this Agreement before an Arbitral Tribunal established under this Article 22 and seek, as a remedy, suitable declaratory relief or monetary compensation. 2. The Parties agree that a Counterclaim made in accordance with this Article 22(G) shall not preclude or operate as res judicata against applicable legal, enforcement or regulatory action in accordance with the laws of the Host State or in any other proceedings before judicial bodies or institutions of the Host State. 3. An initiation of a Counterclaim by a Respondent shall not in itself constitute a waiver of an objection raised by that Respondent to the Arbitral Tribunal's jurisdiction over an Investment Dispute. 	<p>Article 10.30 Counterclaims</p> <ol style="list-style-type: none"> 1. The respondent may submit a counterclaim on the basis of an investor's failure to comply with an international obligation applicable in the territories of both Parties,²⁶ arising in connection with the factual basis of the claim.²⁷ 2. The counterclaim shall be submitted no later than in the Respondent's counter-memorial or statement of defence, or at a later stage in the proceedings if the Tribunal decides that the delay was justified under the circumstances. 3. For greater certainty, claimant's consent to the procedures under this Section includes the submission of counterclaims by the respondent. <p>²⁶ For greater certainty, the obligations referred to in this paragraph shall be based on legal commitments that the Parties have consented to.</p> <p>²⁷ The Joint Council/ Committee shall, at the request of a Party, issue binding interpretations pursuant to article [insert] to clarify the scope of international obligations that are referred to in this paragraph.</p>

¹⁵⁰ Original text in French: “28.4 Lorsqu’un investisseur ou son investissement ne s’est pas acquitté des obligations qui lui incombent en vertu de l’article 18 (Respect des lois internes et des obligations internationales) ou a violé l’article 19

Appendix 2: Provisions Including Investor Obligations

Treaty and Article	Provisions Including Investor Obligations
ECOWAS Supplementary Act (2008)	Article 11: General Obligations Article 12: Pre-Establishment Impact Assessment Article 13: Anti-Corruption Article 14: Post-Establishment Obligations Article 15: Corporate Governance and Practices Article 16: Corporate Social Responsibility Article 17: Investor Liability
Slovakia–Iran BIT (2016)	Article 10(3): Environmental and Labor Rights and Other Standards
Draft Pan-African Investment Code (PAIC) (2016)	Article 19: Framework for Corporate Governance Article 20: Socio-political Obligations Article 21: Bribery Article 22: Corporate Social Responsibility Article 23: Obligations as to the Use of Natural Resources Article 24: Business Ethics and Human Rights
Southern African Development Community (SDAC) Model BIT (2017)	Article 10: Common Obligation against Corruption Article 11: Compliance with Domestic Law Article 12: Provision of Information Article 13: Environmental and Social Impact Assessment Article 14: Environmental Management and Improvement Article 15: Minimum Standards for Human Rights, Environment and Labour Article 16: Corporate Governance Standards Article 17: Investor Liability Article 18: Transparency of Contracts and Payments
Common Market for Eastern and Southern Africa	Article 16: Movement of Labour

(Lutte contre la corruption, le blanchiment des capitaux et le financement du terrorisme), la Partie Hôte peut déposer une demande reconventionnelle devant tout tribunal établi conformément à la présente Section.” English translation available at <https://edit.wti.org/document/show/b5908c50-ef94-4902-b71d-12024f285ef8> accessed 10 December 2022.

(COMESA) Investment Agreement (2017)	<p>Article 25: Compliance with Domestic Measures</p> <p>Article 26: Framework for Corporate Governance</p> <p>Article 27: Socio-Political Obligations</p> <p>Article 28: Bribery and Corruption</p> <p>Article 29: Business Ethics and Human Rights</p> <p>Article 30: Corporate Social Responsibility</p> <p>Article 31: Environmental Protection and Social Impact Assessment</p> <p>Article 32: Environmental Management and Improvement</p> <p>Article 33: Implications of Breach of Investors' Obligations</p>
CPTPP (2018)	Article 9.17: Corporate Social Responsibility
Argentina–UAE BIT (2018)	<p>Article 14: Compliance with the Laws of the Host State</p> <p>Article 17: Corporate Social Responsibility</p>
BLEU Model BIT (2019)	Article 18: Corporate Social Responsibility
Morocco Model BIT (2019)	<p>Article 18: Compliance with Domestic Laws and International Obligations</p> <p>Article 19: Fight Against Corruption, Money Laundering and Terrorist Financing</p> <p>Article 20: Social and Environmental Responsibility</p>
African Arbitration Academy (AAA) Model Bilateral Investment Treaty for African States (2022)	<p>Article 9: Investment and Environment</p> <p>Article 10: Investment, Labour, Human Rights Protection and Gender Equality</p> <p>Article 11(B): Protection of Indigenous Peoples and Local/Ethnic Communities' Rights and Resources</p> <p>Article 12: Anti-Corruption, Anti-Money Laundering and Counter-Terrorism Financing</p> <p>Article 13: Corporate Governance and Practices</p> <p>Article 14: Entry and Exit of Foreign Nationals</p> <p>Article 15: Compliance with Domestic Laws</p> <p>Article 18: Corporate Social Responsibility</p>

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