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Counterclaims in treaty-based investment arbitration

An analysis of two main requirements for their admission

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LIST OF ABBREVIATIONS

BIT	Bilateral Investment Treaty
Cocobod	Ghana Cocoa Board
COMESA	Common Market for Eastern and Southern Africa
ECT	Energy Charter Treaty
ICC	International Chamber of Commerce
ICJ	International Court of Justice
ICSID	International Centre for Settlement of Investment Disputes
IIA	International Investment Agreement
NAFTA	North America Free Trade Agreement
SCC	Stockholm Chamber of Commerce
SOCAR	State Oil Company of Azerbaijan Republic
TPP	Trans Pacific Partnership
UNCITRAL (1976)	UNCITRAL Arbitration Rules adopted in 1976
UNCITRAL (2010)	UNCITRAL Arbitration Rules as revised in 2010
UPICC	UNIDROIT Principles of International Commercial Contracts
VCLT	Vienna Convention on the Law of Treaties

I. INTRODUCTION

A counterclaim is a retaliatory claim asserted by a respondent against a claimant. It is not the same as a statement of defense. In the latter a respondent rebuts claimant's arguments thereby denying any breach allegedly committed by him. To put another way, in defense a respondent denies the cause of action, in counterclaim though it asserts a separate cause of action.[1] A counterclaim therefore should rather be characterized as a counter-attack than defense.

Unlike commercial arbitration and litigation where a respondent is usually entitled to raise a counterclaim, the issue of counterclaims in treaty-based investment arbitration is problematic. This mainly stems from the very nature of treaty arbitration, that operates as a triangular system where home and host states conclude IIA and an investor benefits from provisions of that IIA. This triangularity often leads to asymmetry of procedural rights, where only an investor may sue a host state but not vice versa. This asymmetry in its turn often leads to deprivation of the right to raise counterclaims against investors. Nevertheless, counterclaims have great importance in treaty arbitration which may be underlined by the following.

First of all, the issue of counterclaims in treaty arbitration is a new phenomenon. Presumably this is the reason why this matter is not uniformly regulated. For example, the first counterclaim in treaty arbitration was asserted in *Genin v Estonia* case (Award of 2001)[2], however in contract-based investment arbitration it occurred much earlier: in *Adriano Gardella S.p.A v Republic of Ivory Coast case* (Award of 1977).[3] Most of the treaty arbitration cases where the host states counterclaimed against the investors have been decided within the last five years.[4]

Secondly, counterclaims are highly rare in treaty arbitration. According to UNCTAD data to date there are over 700 treaty-based investor-state arbitrations[5], however the number

[1] Alison Dundes Renteln, "Encountering Counterclaims", *Denver journal of International Law and Policy 15* (1986): 380.
[2] Dafina Atanasova, Carlos Adrian Martinez Benoit and Josef Ostřanský, "Counterclaims in Investor-State Dispute Settlement (ISDS) under International Investment Agreements (IIAs)", Graduate Institute Centre For Trade And Economic Integration (2012): Annex, Table 4.
[3] Mark Friedman and Ina Popova "Can State Counterclaims Salvage Investment Arbitration?" *World Arbitration & Mediation Review 8* (2014) 139 – 179
[4] Kelsey Brooke Farmer, "The Best Defence is a Good Offense – State Counterclaims in Investment Treaty Arbitration" (LLM Research Paper, Victoria University of Wellington, 2016), 4, http://hdl.handle.net/10063/5004
[5] Data is taken from http://investmentpolicyhub.unctad.org/

of those where states counterclaimed against investors does not exceed fifteen[6]. So far only in one case the counterclaim succeeded.[7]

Third, counterclaims bear multiple tasks in treaty-based investment arbitration. It is a legal tool that increases judicial efficiency by "coordinating the handling of multiple claims at once".[8] Considering a primary claim and a counterclaim in the same fora guarantees consistent results which would not be insured in case of separate review of those claims.[9] Counterclaims therefore allow a respondent to seek justice in the same fora avoiding further appeal to litigation.[10] Also, a counterclaim may avail to avoid financial losses incurred due to delay between the adjudication of a primary claim and a counterclaim.[11] Furthemore, a counterclaim may as well facilitate a more fair result by ensuring that additional facts are not omitted.[12]

Fourth, counterclaims in treaty-based investment arbitration may become an efficient instrument against investors' breaches. The fear of being sued by a host state might make investors act in compliance with host state's law. Investor's therefore may refuse to file a claim to arbitration if they anticipate encountering counterclaims.[13] For states a counterclaims may also serve as a tool by which they will clear their reputation damaged by unfounded allegations put forward by investors.[14]

The practice shows that counterclaims in treaty arbitration are allowed in principle.[15] However their admission depends upon certain factors: (i) counterclaims must fall under disputing parties' (state's and investor's) consent and (ii) they must have close connection with the primary claim. This Thesis analyzes consent and connectedness requirements for the admission of counterclaims in treaty-based investment arbitration and the practical importance of why these requirements should be distinguished from one another.

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[6] Atanasova, Benoit and Ostřanský, "Counterclaims in ISDS", Annex, Table 4.
[7] *Burlington Resources Inc. v. Republic of Ecuador*, ICSID Case No. ARB/08/5, Decision on Ecuador's Counterclaims, 7 February 2017. The Tribunal ordered Burlington to pay environmental damage in an amount of USD 39,199,373.
[8] Renteln, "Encountering Counterclaims", 380.
[9] Ibid.
[10] Guido Carducci, "Dealing with Set-off and Counterclaims in International Commercial and Investment Arbitration", *Transnational Dispute Management* 4 (2012): 2, www.transnational-dispute-management.com/article.asp?key=1867
[11] Renteln, "Encountering Counterclaims", 380.
[12] Ibid.
[13] Ibid, p.379.
[14] Ibid, pp. 379-380.
[15] Farmer, "A Good Defence", 4

II. CONSENT AS A CORNERSTONE FOR THE JURISDICTION OVER COUNTERCLAIMS

To date only few IIAs address the issue of counterclaim[16], the rest are silent on this matter.[17] As stated above, two main elements are necessary to accept the counterclaims advanced by a state: parties' consent and connectedness between the principal claim and a counterclaim. At the same time, some treaties may impose additional requirement with regard to this issue.[18]

This Chapter focuses on the issue of consent to counterclaims in treaty-based investment disputes, which is a precondition for the exercise of jurisdiction over counterclaims. Before analyzing the very consent from various angles, it is preferable[19] to start with the determination that consent refers to the jurisdictional matters, as long as this determination has practical significance.

2.1. Consent as a jurisdictional issue

Despite the equal necessity of both consent and connectedness requirements for the admission of a counterclaim, they relate to different concepts. Consent is the element which conditions the jurisdiction of the tribunal and consequently relates to the jurisdictional matters.

Where the jurisdiction of a tribunal or court rests on the agreement of parties, parties' consent should be a key element for asserting that jurisdiction. ICJ established the foundational rule that consent is the cornerstone of its jurisdiction.[20]

Similar notion finds its reflection in the Report of Executive Directors on the ICSID Convention, underlining that consent of the parties is the cornerstone of the jurisdiction of the Centre.[21] The whole dispute resolution process under ICSID Convention rests on the parties' consent: it is a necessary condition for ICSID jurisdiction that both parties consent to submit

[16] See for example Investment Agreement for the COMESA Common Investment Area (2007) or Trans Pacific Partnership (2016).
[17] See for example Chile-Norway BIT (1993), Argentina-Canada BIT (1991), Azerbaijan-BLEU BIT (2004).
[18] Article 46 of the ICSID, in addition to the consent and connectedness, requires, that counterclaim be "within the jurisdiction of the Center".
[19] See Sections 3.4 and 3.5
[20] Michael Waibel, "Corfu Channel Case" in *Max Planck Encyclopaedia of Public International Law*, ed. Wolfrum Rüdiger, (Oxford University Press, 2010): para. 21. The relevance of ICJ to investor-state arbitration may be explained by the fact that jurisdiction of ICJ like jurisdiction of arbitral tribunal is based on agreement (consent) as well.
[21] International Bank for Reconstruction and Development, Report of the Executive Directors on the Convention on the Settlement of Investment Disputes between States and Nationals of Other States (18 March 1965), para. 23

the dispute to the Centre.[22] Schreuer is also of opinion that "consent to arbitration by the host State and by the investor, is an indispensable requirement for a tribunal's jurisdiction."[23]

When it comes in particular to counterclaims "there is a general understanding that for them to be admitted they must fall within the jurisdiction of the particular tribunal, i.e. within the consent of the parties to arbitrate".[24] In *Metal-Tech v Uzbekistan* the Tribunal noted that

> the first requirement [the counterclaim must be within the jurisdiction of the Centre] relates to jurisdiction and, in this respect, singles out the condition of consent. [25]

Similarly, in *Rusoro v Venezuela* the Tribunal confirmed this approach by stressing that the "scope of arbitration agreement" (i.e. scope of consent) is a precondition to assert its jurisdiction over counterclaims.[26] Therefore if the counterclaim is not encompassed by the parties' consent, then it is not arbitrable at all.

However consent in treaty-based investment arbitration is a unique phenomenon. It is reached through a two-step process that involves a state's offer given via BIT and an investor's acceptance of this offer. An offer to arbitrate and an investor's acceptance will be addressed in Sections 2.2 and 2.3 respectively.

2.2. Host state's offer to arbitrate

Arbitration is based on the will of the parties[27]: it rests on the offer and the acceptance. If one of these elements lacks, there is no basis for arbitration. In contract-based investment arbitration, offer-acceptance process is clear-cut, as long as the parties reach directly an agreement on arbitration.[28] For example, Production Sharing Agreement between SOCAR (Azerbaijan Republic) and other oil companies states that

> all disputes arising between SOCAR and any or all of the Contractor Parties, including without limitation, any dispute as to the validity, construction, enforceability or breach of this Contract… shall be finally settled before a panel of three (3) arbitrators under the Arbitration

[22] Oscar Garibaldi, "On the Denunciation of the ICSID Convention, Consent to ICSID Jurisdiction, and the Limits of the Contract Analogy", *Transnational-Dispute Management* 1 (2009): 8, www.transnational-dispute-management.com/article.asp?key=1339

[23] Christoph Schreuer, "Consent to Arbitration", (updated 02/ 2007), *Transnational Dispute Management 5* (2007): 1, www.transnational-dispute-management.com/article.asp?key=555

[24] Atanasova, Benoit and Ostřanský, "Counterclaims in ISDS", 12.

[25] *Metal-Tech Ltd v The Republic of Uzbekistan*, ICSID Case No. ARB/10/3, Award, 04 October 2013, paras. 407-408.

[26] *Rusoro Mining Ltd. v. Bolivarian Republic of Venezuela*, ICSID Case No. ARB (AF)/12/5, Award of 22 August 2016, paras. 619-620.

[27] Giuditta Cordero-Moss, *International Commercial Contracts*, (Cambridge University Press, 2014): 211, para.2.

[28] According to Article 2 of the New York Convention On The recognition and Enforcement of Foreign Arbitral Awards, agreement on arbitration includes an arbitration clause as well.

Rules of The United Nations Commission on International Trade Law known as UNCITRAL (the "Rules").[29]

This is a clear illustration of "arbitration with privity", when both the state and investor(s) reach an agreement on arbitration directly. The word "privity", defines relationship between persons who have a legal interest in the same right or property.[30]

However, in treaty-based investment dispute the mechanism of reaching an agreement on arbitration between a state and an investor is different. A state and an investor do not come into direct contact for the conclusion of arbitration agreement by reason that IIAs are concluded between home and host state of the investor, i.e. the investor is not a party to IIA. However, absent any direct agreement on arbitration with a host state, an investor may nevertheless initiate proceedings by invoking IIA clause. This mechanism is generally called "arbitration without privity"[31].

As a first step for the arbitration, a state makes its offer to arbitrate in IIA. Nolan considers this offer as the one "similar to offers to enter into contract".[32] According to his opinion a "[c]onsent to arbitrate, thus becomes a multi-stepped process, beginning with an offer of arbitration by the state which is perfected by means of an acceptance by an investor".[33]

Often but not always, states endorse their offer to arbitrate by giving unequivocal consent to arbitration. This consent is given through the formulation in IIAs like "each Contracting Party hereby consents to the submission of an investment dispute by a disputing investor to arbitration…"[34] Other IIAs have the same or at least similar wording as to the consent of the state.[35] Some IIAs[36] envisage the undertaking of a state to give its "future" consent to arbitration if any dispute arises, thereby promising to respond to investor's request

[29] The Production Sharing Agreement (Azeri-Chirag-Deepwater Gunashli) of 1994, Appendix VI (Arbitration), para. 1.1.
[30] İnci Ataman-Figanmeşe, "Manufacturing Consent to Investment Treaty Arbitration By Means of the Notion of "Arbitration Without Privity", *Annales de la Faculté de Droit d'Istanbul*, No. 60 (2011): 193.
[31] Ibid.
[32] Frederic Sourgens and Michael Nolan, "Limits of Consent - Arbitration Without Privity and Beyond", *Liber Amicorum Bernardo Cremades (Kluwer 2010)*: 2, https://ssrn.com/abstract=2180302
[33] Ibid, 2-3
[34] See for example, Canada-Uruguay BIT (1997) or Azerbaijan-USA BIT (1997).
[35] See for example Canada-Kuwait BIT (2011) stating *"[e]ach Party consents to the submission of a claim to arbitration in accordance with the terms of this Agreement;* Romania-Canada BIT (2009) stating *"[e]ach Contracting Party … gives its unconditional consent to the submission of a dispute to international arbitration";* USA-Lithuania BIT (1998) stating *"[e]ach Party hereby consents to the submission of any investment dispute for sectlement by binding arbitration".*
[36] See for example, Japan-Pakistan BIT (1998), Aritcle 10(2)

to initiate arbitration.[37] However a mere promise to give consent may hardly be tantamount to the very consent.[38]

A state may make its offer to arbitrate through its municipal law as well. However, there are distinctive characteristics between the offer made by municipal law and the one included in a treaty. National law on investment protection provides this offer to all the investors, independently of the country of origin. In a treaty however, contracting parties give their consent to arbitrate only to each other's investors, thereby, excluding investors of other countries from enjoyment of the right to sue the state.

To summarize, the consent in treaty-based investment arbitration is a two-step process and the host state's offer to arbitrate is only the first step. For the arbitration to take place, that offer must be accepted by an investor.

2.3. Investor's acceptance of the offer

To initiate the arbitral proceeding against a state, an investor must accept state's offer given through the treaty. A dispute resolution clause in a treaty is supposed to be considered as nothing more than a simple offer to arbitrate. It has no binding effect on investor unless he/she accepts that offer.

Steingruber mentions several ways as to the expression of investor's acceptance: by instituting the proceeding and prior to it.[39] In most, if not all, of the cases after expiration of cooling-off period investors start proceedings by the mere referring to arbitration without sending any prior notice to a respondent state on the intention to initiate arbitration. In case *Generation Ukraine Inc. v Ukraine*, the Tribunal stressed:

> [i]t is firmly established that an investor can accept a State's offer of ICSID arbitration contained in a bilateral investment treaty by instituting ICSID proceedings.[40]

In practice, if IIA does not precisely envisage otherwise, institution of arbitral tribunal suffices for the acceptance of the offer. In *Generation Ukraine* case, the Tribunal further noted:

> There is nothing in the BIT to suggest that the investor must communicate its consent in a different form directly to the State; to the contrary, the express language of Article VI(3)(a) dictates otherwise.[41]

[37] Schreuer, "Consent to Arbitration", 7.
[38] Ibid, p.7
[39] Andrea Marco Steingruber, *Consent in International Arbitration* (Oxford University Press, 2012): 206-207.
[40] *Generation Ukraine Inc. v Ukraine*, ICSID Case No. ARB/00/9, Award, 16 September 2003, para. 12.2.
[41] Ibid, para. 12.2

Therefore, absent any special requirements as to the expression of an investor's acceptance, the mere institution of arbitration suffices for a state's offer to be deemed accepted.

Some IIA require that an investor give its written consent before initiating proceedings. For instance, Canada-Phillipines BIT (1995) provides:

> An investor may submit a dispute … to arbitration in accordance … only if:
> (a) the investor has consented in writing thereto…[42]

Under such BIT the mere reference to arbitration by an investor after the expiration of cooling-off period may not be amounted to acceptance of host state's offer to arbitrate. Investor's acceptance of host state's offer should be in writing.

Steingruber brings an interesting example, where investor's consent may be ignored by a host state while initiating the proceedings.[43] France-Nigeria BIT (1990) Article 8 states, that in case of non-settlement of a dispute between a state and an investor, each party may submit a case to the arbitration. Under this BIT, if an investor brings a case before arbitration, there is nothing problematic. The offer to arbitrate is given and initiation of arbitration by an investor amounts to acceptance of that offer. However, if under this BIT a state starts arbitration against an investor (the wording of the BIT enables a state to do so), this means that the state accepts its own offer to arbitrate, thereby breaching offer-acceptance process. One can hardly disagree with Streingruber's opinion, that the formulation in that BIT is "flawed",[44] as long as the absence of investor's acceptance makes the core of the arbitration insubstantial. Ignoration of the investor's consent, indeed, means that no agreement on arbitration is reached between the parties, consequently, no arbitral proceeding may be initiated. Therefore, language of IIA should be free of ambiguity, expressly or at least impliedly providing for the possibility of arbitration only upon investor's acceptance.

To sum up, in order to assert jurisdiction over a dispute a tribunal must be assured that the offer to arbitrate given via IIA is duly accepted by an investor. Reaching an agreement on arbitration through both parties' consent does not suffice for the admission of counterclaims. The acceptance of counterclaims will depend upon the scope of that consent.

2.4. Scope of consent

This part of the Thesis, comes close to the main issue, i.e. to counterclaims. The fact that a tribunal has jurisdiction over a claim of an investor does not necessarily mean that this

[42] Canada-Philippines BIT (1995), Article 13. See also Canada-Ukraine (1994) BIT, Article 13
[43] Steingruber, *Consent in International Arbitration*, 207
[44] Ibid.

jurisdiction extends over host state's counterclaims as well. Since arbitration rests on the consent of the parties, then this consent conditions counterclaims too.[45] Hence, in order to be admitted by tribunal counterclaims should fall within the scope of that consent.

What makes the consent requirement so specific in treaty-based investment arbitration is that its scope is not mutually agreed between parties. Indeed, a state is the one, who "sets the rule of the game" by determining how broad the offer is.[46] This offer further affects the eligibility of a state to bring counterclaims against an investor. Accordingly, if a state wants to advance counterclaims, it has to incorporate the possibility of these counterclaims into its offer to arbitrate. The Tribunal in *Roussalis v Romania* noted that

> The investor's consent to the BIT's arbitration clause can only exist in relation to counterclaims if such counterclaims come within the consent of the host State as expressed in the BIT.[47]

Likewise, in *Metal-Tech v Uzbekistan* the Tribunal pointed:

> The scope of the State's offer is defined in the investment treaty, in particular in the dispute resolution clause of that treaty. When he initiates an arbitration under the treaty, the investor accepts the offer within the scope defined in the treaty.[48]

These notions in fact mean, that if a state asserts counterclaims, it has to prove, that it consented to these counterclaims beforehand, i.e. they were included in the offer to arbitrate.

In order to enable a state to advance a counterclaim this offer must be accepted by an investor. What if an investor accepts the offer of the state, but not in its entirety, i.e. excluding the terms on counterclaims? May the investor limit the scope of state's offer so that to deprive that state of the right to advance a counterclaim?

In fact, investor's acceptance of this offer is of limited role. An investor may only accept or reject the host state's offer, but may not limit or enlarge it, i.e. go beyond the borders of state's consent.[49] By initiating an arbitral proceeding against a host state an investor thereby accepts the state's offer as set out in the treaty, nothing more and nothing less.[50] Lalive was also of the opinion, that:

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[45] ICSID Convention, Article 46 and ICSID Arbitration Rules, Article 40(1). See also *Spyridon Roussalis v. Romania*, ICSID Case No. ARB/06/1, Award, 7 December 2011 and *Saluka Investments B.V. v Czech Republic*, UNCITRAL, Decision on Jurisdiction Over the Czech Republic's Counterclaim.

[46] Andrea Marco Steingruber, "Antoine Goetz and others v Republic of Burundi: Consent and Arbitral Tribunal Competence to Hear Counterclaims in Treaty-based ICSID Arbitrations (Case Comment)", *ICSID Review* 28, No. 2 (2013): 299, doi:10.1093/icsidreview/sit017

[47] *Roussalis v Romania*, para. 866.

[48] *Metal-Tech v Uzbekistan*, para. 409.

[49] Steingruber, *Consent in International Arbitration*, 300.

[50] Hege Elisabeth Kjos, "The Scope of the Arbitration Agreement: Claims and Counterclaims of a National and/or International Nature" in *Applicable Law in Investor-State Arbitration: The Interplay between National and International Law* by Hege Elisabeth Kjos (Oxford University Press, 2013): 135.

> The investor cannot pick and choose from the dispute resolution provision of a BIT, just like it cannot pick and choose from other provisions of the investment agreement. A BIT is not an *a la carte* selection of provisions among which the investor can choose – deciding, for example, to arbitrate its own expropriation claim but not the state's "essential security interests" defence. The offer to arbitrate in a BIT's dispute resolution provision can only be accepted according to its own terms.[51]

Similar idea was underlined in *Urbaser v Argentina* case. The Tribunal on the possibility of the investor's restricted acceptance noted:

> Even if it is argued that Claimants' acceptance was more restricted in its scope than the Argentine Republic's offer to arbitrate contained in Article X of the BIT, the appropriate conclusion would have been that no agreement had been concluded between the Parties.[52]

Accordingly, state's offer envisaged in investment treaty is a "take or leave" option, meaning that the investor may not expand or limit the host state's standing offer to arbitrate in the IIA.[53] Limited acceptance by an investor may be qualified as a counteroffer, i.e. a rejection, rather than an acceptance of the offer.[54]

As stated above, arbitration is based on agreement. Some authors therefore treat state's offer to arbitrate as an offer to enter into contract.[55] Taking this into account these factors, I will endeavor to analyze the limited acceptance of state's offer in the context of UPICC. It states that

> [a] reply to an offer which purports to be an acceptance but contains additions, limitation or other modifications is a rejection of the offer and constitutes a counter-offer.[56]

But

> ..a reply to an offer which purports to be an acceptance but contains additional or different terms which do not materially alter the terms of the offer constitutes an acceptance, unless the offeror, without undue delay, objects to the discrepancy.[57]

Therefore, if to interpret state's offer in the view of UPICC an investor is not eligible to limit or extend the scope of the state's offer, unless the modification materially alters the conditions set in the treaty. UPICC defining material modification states:

> What amounts to a "material" modification cannot be determined in the abstract but will depend on the circumstances of each case. Additional or different terms relating to the price or mode of payment, place and time of performance of a non-monetary obligation, the extent of one party's

[51] Pierre Lalive and Laura Halonen, "On the Availability of Counterclaims in Investment Treaty Arbitration", *Czech Yearbook of International Law*, (eds) Alexander Belohlávek and Nadežda Rozehnalová, Vol.2 (2011): 150, para. 7.30

[52] *Urbaser S.A. and Consorcio de Aguas Bilbao Bizkaia, Bilbao Biskaia Ur Partzuergoa v. The Argentine Republic*, ICSID Case No. ARB/07/26, Award, 8 December 2016, para.1147.

[53] Steingruber, "Comments on Goetz v Burundi case", 297.

[54] Kjos, "The Scope of the Arbitration Agreement", 136.

[55] See above n. 32.

[56] UPICC (2010), Article 2.1.11(1)

[57] Ibid., Article 2.1.11(2)

> liability to the other *or the settlement of disputes*, will normally, but need not necessarily, constitute a material modification of the offer.[58]

The modification of the offer, made by excluding the eligibility of the state to bring counterclaims, should be considered as "material", as long as it limits the procedural rights of the state in arbitration as such, thereby depriving that state of the main title: to bring its own claims against the claimant in case of alleged violations committed by the latter. Therefore, from position of UPICC, restricted acceptance of state's offer amounts to a material modification, which means that the agreement on arbitration is not reached.

To sum up all the above-mentioned, a state is a key figure, that sets the borders of the consent and investor's acceptance must exactly correspond to its limits. The investor may neither extend, nor restrict the scope of the consent proposed by that state, otherwise this will be tantamount to the counter-offer, i.e. to the rejection of that offer.

2.5. Interpretation of the scope of consent

In treaty-based arbitration as a starting point for the derivation of the parties' consent, a tribunal should refer to the IIA itself. It is a primary source, which contains an offer of the state to arbitrate and entitles an investor to bring its claim against that state by accepting the offer. Subsection 2.6.1 will explore the primacy of IIA over other instruments. This Section though focuses on the interpretation of IIA, to be more precise on interpretation of the scope of consent.

As long as a state's consent is given through IIA, the fate of counterclaims will depend upon the tribunal's interpretation of IIA. The interpreter's (tribunal's) first and foremost task here is to determine the limits of parties' consent, what in its turn will lead to the conclusion on whether this consent encompasses counterclaims or not. Like all the treaties IIAs are supposed to be interpreted in accordance with the Vienna Convention on the Law of the Treaties. Article 31(1) of VCLT states that "[a] treaty shall be interpreted in good faith in accordance with the *ordinary meaning* to be given to the terms of the treaty in their context and *in the light of its object and purpose*".[59] For instance, the Tribunal in *Roussalis v Romania* interpreted the state's consent in the Greece-Romania BIT (1997) in accordance with Article 31(1) of VCLT, ultimately finding no basis for jurisdiction over the counterclaims:

> Pursuant to the interpretation rules of Article 31 of the Vienna Convention and the above quoted ICSID decision, the Tribunal in its majority considers that the references made in the text of

[58] Ibid., Comment 2 to Article 2.1.11
[59] VCLT, Article 31(1).

> Article 9(1) of the BIT to "*disputes ... concerning an obligation of the latter"* undoubtedly limit jurisdiction to claims brought by investors about obligations of the host State.[60]

If counterclaims are expressly permitted under IIA[61], then there is no complexity as to the assertion of jurisdiction over those counterclaims. Accordingly, in such a scenario a claimant is unlikely to deny that by instituting arbitration it did not consent to counterclaims. Complication though arises when the tribunal has to deal with IIA containing no express reference to counterclaims.[62] Do IIAs of this kind exclude the possibility of counterclaims at all? According to case study the answer is negative. A tribunal must construe a treaty rule so that to give that rule an effective meaning.[63] This effectiveness may be reached by avoiding an "interpretation which leads to either an impossibility or absurdity or empties the provision of any legal effect".[64] The language of IIA may enable the admission of counterclaims despite the absence of explicit reference to them.[65]

Hence, while interpreting the state's offer to arbitrate, a tribunal may focus on specific IIA provisions which may indicate the possibility or impossibility of counterclaims. Subsections below will discuss some of these provisions.

2.5.1. *"(all, any) dispute(s)… concerning an investment"*

Dispute resolution clauses included in IIAs vary in terms of the scope of *ratione materiae.* Some treaties provide for quite broad basis of subject-matter jurisdiction. For instance, Spain-Albania BIT's dispute settlement clause encompasses

> *Disputes* between an investor of one Party and the other Party *concerning an investment*…[66]

Another example is Argentina-Finland BIT which includes

> *Any dispute …concerning an investment* between an investor of one contracting Party and the other Contracting Party.[67]

Pursuant to Tribunals' interpretations in *Saluka*[68] and *Paushok*[69] cases the term *"all disputes" (or "disputes")* embodies not only the claims of investor, but state's counterclaims as well.

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[60] *Roussalis v Romania*, para. 869.
[61] See for example Trans Pacific Partnership (2016), Chapter 9, Section B, Article 9.19 or Investment Agreement for the COMESA Common Investment Area (2007), Article 28(9).
[62] See for example, France-Mexico BIT (1998), Energy Charter Treaty (1994), Germany-Ghana BIT (1995), USA-Uruguay BIT (2005).
[63] *Urbaser v. Argentina*, para.1190.
[64] Ibid.
[65] See *Saluka v Czech Republic*, and *Sergei Paushok et al v The Government of Mongolia*, UNCITRAL, Award on Jurisdiction and Liability, 28 April 2011.
[66] Spain-Albania BIT (2003), Article 11.
[67] Argentina-Finland BIT (1993), Article 13. See also Czech and Slovak Federal Republic – Norway BIT (1991), Denmark – Russia BIT (1993).
[68] *Saluka v Czech Republic*.

Despite the fact that there is no case law in its strict sense in investment arbitration, the cases below nevertheless demonstrate that tribunals tend to admit counterclaims, when they deal with the IIAs which include formulation *"(all) disputes concerning investment"*.

One of the investor-state disputes, where the issue of consent to counterclaims was addressed was *Saluka v Czech Republic* case. The dispute arose out of the privatization of one of the biggest at the time Czech banks, namely Investicní a Poštovní Banka A.S. (IPB) and was decided under the UNCITRAL Arbitration Rules (1976). The BIT in question in Article 8 stated, that

> (1) All disputes between one Contracting Party and an investor of the other Contracting Party concerning an investment of the latter shall if possible, be settled amicably.
> (2) Each Contracting Party hereby consents to submit a dispute referred to in paragraph (1) of this Article, to an arbitral tribunal, if the dispute has not been settled amicably within a period of six months from the date either party to the dispute requested amicable settlement.[70]

Claimant noted, that Respondent's offer to arbitrate, in Article 8 above, included only claims of the investor and there was no consent as regards to counterclaims.[71] However, Tribunal examined this provision along with UNCITRAL Arbitration Rules (1976) and concluded:

> …in principle, the jurisdiction conferred upon it by Article 8, particularly when read with Article 19.3, 19.4 and 21.3 of the UNCITRAL Rules, is in principle wide enough to encompass counterclaims. The language of Article 8, in referring to "All disputes," is wide enough to include disputes giving rise to counterclaims, so long, of course, as other relevant requirements are also met.[72]

Eventually, the Tribunal dismissed the counterclaims, but rather on other grounds, than the absence of consent.

Thus, according to the Tribunal, the wording "all disputes" included not only claims of the Claimant, but the Respondent's counterclaims as well. In its view, by submitting the claims against the State, Saluka *ipso facto* consented to the possible submission of counterclaims. *Saluka* was the first case where the Tribunal interpreted broad formulation of *ratione materiae* as the one permitting counterclaims. This approach later on was applied in other cases.[73]

In *Paushok v Mongolia* case the Tribunal took similar approach. The dispute concerned the operation of gold mining company in Mongolia. The Claimants (Mr. Sergei Paushok,

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[69] *Paushok v Mongolia*.
[70] Netherlands – Czech and Slovak Republic BIT (1991), Article 8
[71] *Saluka v Czech Republic*, para. 26.
[72] Ibid. para.39
[73] See *Pasuhok v Mongolia* and *Metal-Tech v Uzbekistan.*

CJSC Golden East Company and CJSC Vostokneftegaz Company) alleged, that Mongolia had breached Articles 2, 3 (Treatment) and 5 (Expropriation) of the Russia – Mongolia BIT by adopting new laws, including Law on "On Imposition of Price Increase (Windfall) Taxes on Some Commodities" (WPT Law) and the Law "On Minerals".[74] The dispute resolution clause in the BIT was alike the one in *Saluka* case:

> Disputes between one of the Contracting Parties and an investor of the other Contracting Party, arising in connection with realization of investments…[75]

Thus, instead of "all disputes", this BIT used the term "disputes". The Tribunal noted that:

> Article 8 of the Saluka BIT is similar to Article 6 of the Treaty, the first one referring to "all Disputes" while the second refers to "disputes" and there is no reason to make a difference between the two.[76]

The Tribunal though did not analyze the issue of the consent to counterclaims in detail. It took the *Saluka* case's approach, concluding, that the terms *"all disputes"* and *"disputes"* enabled the Respondent to bring the counterclaim. Despite the Claimants' objections, Tribunal decided that the consent on counterclaims had been reached.

Another case where the Tribunal had to deal with a broad formulae of *ratione materiae* was *Metal-Tech v Uzbekistan.* The dispute came up between the parties to the joint venture involved in the production of molybdenum in Uzbekistan. Metal-Tech claimed that Uzbekistan violated investment protection standards of Israel-Uzbekistan BIT by (i) expropriating Metal-Tech's investment, (ii) failing to accord fair and equitable treatment to Metal- Tech's investment, (iii) subjecting Metal-Tech's investment to unreasonable and discriminatory measures and (iv) failing to accord full protection and security to Metal-Tech's investment.[77] Uzbekistan as a Respondent filed counterclaims to recover damages sustained as a direct result of Claimant's unlawful conduct.[78] The dispute resolution clause of the BIT in question encompassed *"any legal dispute"* arising between the host state and an investor concerning an investment of the latter.[79] The Tribunal interpreted this provision by stating that

> Article 8(1) of the BIT is not restricted to disputes initiated by an investor against a Contracting Party. It covers *any* dispute about an investment.[80]

[74] *Paushok v Mongolia*, para. 11.
[75] Russia – Mongolia BIT (1995), Article 6
[76] *Paushok v Mongolia*, para. 689.
[77] *Metal-Tech v Uzbekistan*, para. 108
[78] Ibid, para. 110.
[79] Israel-Uzbekistan BIT (1994), Article 8(1).
[80] *Metal-Tech v Uzbekistan*, para. 410.

Therefore, it inferred that the wording of the BIT was broad enough to encompass counterclaims too. However, the Tribunal ultimately dismissed counterclaims of Uzbekistan on the grounds, that

> the Claimant's "investment" [did] not meet the legality requirement and thus [did] not constitute an investment in the meaning of the BIT. In other words, the State's offer to arbitrate did not extend to this "non-investment" and the investor's acceptance included this limitation.[81]

Saluka, *Paushok* and *Metal-Tech* cases clearly demonstrate that broad formulation of *ratione materiae* like *"(all, any) dispute(s) concerning an investment"* enables a respondent party to bring its counterclaims. If the BITs in these cases in their dispute resolution clauses stipulated instead of *"(all, any) disputes"* the phrase *"dispute… concerning the obligations under this Treaty (or Agreement)"*, the Tribunals would have hardly accepted, that this wording embodied consent to counterclaims as well.[82] Consequently, a tribunal should make a distinction between broad and narrow formulation of *ratione materiae*.

2.5.2. *"disputes concerning a breach of obligation of Contracting Party regarding…"*

Other IIAs however provide for a narrower formulation of the term "dispute". These IIAs do not refer to *"any"* or *"all disputes"*, but to disputes arising out of non-fulfillment of obligations by the host state under IIA. For example, France-Mexico BIT's dispute settlement clause "only applies to disputes between a Contracting Party and an investor of the other contracting Party concerning an alleged breach of an obligation of the former" under the BIT.[83] Similarly, Canada-Ukraine BIT sets:

> Any dispute between one Contracting Party and an investor of the other Contracting Party, relating to a claim by the investor that a measure taken or not taken by the former Contracting Party is in breach of [that] Agreement.[84]

The wordings in these BITs may slightly differ, however the core idea remains the same: the dispute may arise only out of the violation of host state's obligations under that BIT.

As long as IIAs generally lay no obligations on investors, a clause that confines the jurisdiction of a tribunal only to claims brought under IIA would most probably hinder assertion of counterclaims by a respondent state.[85] This is due to the fact that "investor's acceptance of state's offer cannot expand its scope to include counterclaims advanced by a

[81] Ibid, para. 411.
[82] Atanasova, Benoit and Ostřanský, "Counterclaims in ISDS", 14.
[83] France-Mexico BIT (1998), Article 9. See also Energy Charter Treaty (1994), Article 26.
[84] Canada-Ukraine BIT (1994), Article 13
[85] Lalive and Halonen, "On the Availability of Counterclaims" para. 7.23.

host state".[86] Where IIA includes only host state's obligations and where disputes under such IIA may arise only out of non-performance of those obligations, then the asymmetry between the procedural rights of an investor and a state is obvious. This asymmetry, where an investor may bring its claim but a state may not disallows counterclaims. Such an asymmetry limits scope of claims arbitrable only to those that advanced by investors, thereby leaving state's counterclaims out of tribunal's jurisdiction. Therefore, by including the limited *ratione materiae* in its offer to arbitrate, which to be either accepted or rejected by an investor, a state thereby deprives itself of the right to counterclaim.

The Tribunal acknowledged this idea in *Roussalis v Romania.* Probably it is the most notorious case of recent years, which caused much controversy. The Tribunal broke new grounds by concluding that "jurisdiction to decide a State's counterclaims is exceedingly narrow".[87] This was the first time that an ICSID tribunal rejected a counterclaim "arising directly out of the subject-matter of the dispute" on the ground that consent requirement was not met.[88] The dispute arose out of the alleged non-performance by the Continent SRL[89] of Privatization Agreement.[90] Turning to the language of dispute resolution clause of the BIT, Tribunal found, that it extended only to the *"disputes between an investor of a Contracting Party and the other Contracting Party concerning an obligation of the latter under [that] Agreement"*.[91] It concluded, that counterclaims remained out of the scope of the consent:

> "disputes ... concerning an obligation of the latter" undoubtedly limit jurisdiction to claims brought by investors about obligations of the host State… The meaning of the "dispute" is the issue of compliance by the State with the BIT.[92]

In *Hamester v Ghana*, the Tribunal considering the issue of counterclaims faced similar wording of BIT as regards to the scope of consent. It emphasized that

> In this case, the scope of consent in Article 12(1) of the BIT is limited to disputes: "concerning an obligation of [one Contracting Party] under [that] Treaty in relation to an investment of [a national or company of the other Contracting Party]."[93]

The Tribunal eventually concluded with regard to the issue of consent, that

[86] Zachary Douglas, *The International Law of Investment Claims* (Cambridge University Press, 2009): para. 491.
[87] Mark Bravin and Alex Kaplan, "Arbitrating Closely Related Counterclaims at ICSID in the Wake of Spyridon Roussalis v. Romania", *Transnational Dispute Management* 4 (2012): 1, www.transnational-dispute-management.com/article.asp?key=1860
[88] Ibid, p.2
[89] Continent SRL was a legal entity fully owned by Spyridon Roussalis. See *Roussalis* case, para. 4.
[90] Privatization Agreement was concluded between Continent SRL and AVAS (or State Property Fund), which was in charge for the privatization of state-owned enterprises. See *Roussalis v Romania*, para. 7.
[91] Hellenic Republic-Romania BIT (1997), Article 9(1)
[92] *Roussalis v Romania*, para. 869.
[93] *Gustav F W Hamester GmbH & Co KG v. Republic of Ghana*, Award, 18 June 2010, para. 353.

> Despite the restricted scope of covered disputes, the BIT recognizes that the State party may be "aggrieved" and "shall have the right to refer the dispute to" arbitration (Article 12(3) and (4) of the BIT).[94]
>
> However, in the absence of any submissions on the nature of the Respondent's counterclaim under the BIT, the Tribunal is unable to analyze whether it is capable, in accordance with Article 46 of the Convention, of falling within the parties" scope of consent.[95]

It found other grounds for the dismissal of the counterclaims. However, Tribunal could have drawn a more precise conclusion as to the consent. The language of Article 12(1) of the BIT sufficed to conclude that the counterclaims fell outside the Treaty and consequently outside the parties' consent. The BIT in question do not encompass the investor's obligations. It explicitly envisages that the dispute may arise only with regard to the state's obligations in relation to an investment of a national or company of the other Contracting Party.[96] Accordingly, any violations committed by the investor may not be disputed under this BIT. Investor is the only party, who enjoys the full set of procedural rights and whose claims are arbitrable under the Treaty.

Similarly, the BIT in *Rusoro v Venezuela* also confined the scope of arbitrable disputes to those which might arise only out of violation of the obligations of the host state under the Treaty:

> Any dispute between one Contracting Party and an investor of the other Contracting Party, 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.[97]

The Tribunal relying on the language of the BIT emphasized that

> The literal wording of [Article 12] does not leave room for doubt: the Treaty affords investors, and only investors, standing to file arbitrations against host States…[98]

Therefore it dismissed Venezuela's counterclaims, due to the reason that only the investor's claims were arbitrable.[99]

So, the cases in this Subsection show that tribunals are keen to dismiss state's counterclaims if dispute resolution clauses in IIAs limit the material scope of disputes only to those arising out of non-fulfillment of obligations by a host-state. It appears that limited *ratione materiae* does not permit tribunals to consider host state's counterclaims.

[94] Ibid, para. 354.
[95] Ibid, para. 355.
[96] Germany-Ghana BIT (1995), Article 9.
[97] Canada-Venezuela BIT (1996), Article 12.
[98] *Rusoro v. Venezuela*, para. 627.
[99] Ibid, para. 678.

2.5.3. *"an investor may submit the dispute to arbitration" v. "either party may submit the dispute to arbitration"*

Another factor that may speak well for or against the possibility of counterclaims is the right of parties to initiate arbitration as expressed in IIAs. Some IIAs provide that only an investor enjoys the right to institute arbitration. Mongolia-Turkey BIT states that if the disputes between the investor and the host state cannot be settled during six months, the investor may choose to submit the case to ICSID, SCC or ad hoc arbitration under UNCITRAL Arbitration rules.[100] Likewise, Argentina-Netherlands BIT grants only the investor the right to initiate arbitral proceedings provided that he/she has already exhausted local remedies.[101] Does the limited *locus standi,* irrevocably and unconditionally deprive a respondent state of the right to counterclaim due to lack of consent? Apparently, the answer is negative.

The limited *locus standi* in IIA may not in itself be seen as an intention of states to limit their own procedural rights.[102] An emphasis on investor's right to initiate proceedings could rather be seen as the host state's willingness to arbitrate and nothing more.[103] So far no decision was made on dismissal of counterclaims solely on the basis of limited *locus standi*. Accordingly, the limited *locus standi* does not serve as a decisive factor for inadmissibility of counterclaims, however combined with limited jurisdiction *ratione materiae*[104] it will have such effect.[105] Where IIA confines the scope of claims arbitrable only to those arising out of violation of obligations under IIA[106] and conferring the standing to initiate arbitration only to investor, then there is no room for counterclaims at all.

By contrast in combination with broad jurisdiction *ratione materiae*[107] the limited *locus standi* will not have any effect at all. It will just be considered by a tribunal as the mere absence of the right to initiate proceedings and nothing more and the absence of this right will not bar the admission of counterclaims. *Saluka* case might be an illustration.[108] Unveiling that only the investor was entitled to start arbitration, the Tribunal nevertheless inferred that the

[100] Mongolia-Turkey BIT (1998), Article 6.
[101] Argentina-Netherlands BIT (1992), Article 10 (3).
[102] Kjos, "The Scope of the Arbitration Agreement", 141
[103] Ibid.
[104] Means the disputes arising only out of violation of host state's obligations under a BIT. See Section 2.5.2
[105] Kjos, "The Scope of the Arbitration Agreement",141
[106] Assuming that BITs generally include only state's obligations.
[107] See Section 2.5.1
[108] See Netherlands – Czech and Slovak Republic BIT (1991), Article 8.

scope of consent was broad enough to include counterclaims as well.[109] Therefore, a limited standing does not solely serve as a determinant for dismissal of counterclaims.

Other IIAs though accord both an investor and a host state the right to initiate arbitral proceedings. For example Canada-Argentina BIT states that "disputes may be submitted to international arbitration by one of the parties to [that] dispute"[110] thereby implying the host state's *locus standi* as well.

A reasonable interpretation of provision of this pattern would be that the host state as a potential claimant having the right to bring its claims may also bring counterclaims.[111] The arguments speaking for the arbitrability of counterclaims are even more convincing when the broad *locus standi* is combined with broad jurisdiction *ratione materiae*. For example, the USA-Estonia BIT states that

> Any dispute between the Parties concerning the interpretation or application of the Treaty which is not resolved through consultations or other diplomatic channels, shall be submitted, upon the request of either Party, to an arbitral tribunal…[112]

Lalive said:

> When the clause refers to claims "arising from investments", and in particular when the clause appears to make it possible for the state to initiate the arbitration as well, a tribunal has no reason not to give effect to the text and purpose of such a clause and find that the state has consented to have such counterclaims arbitrated.[113]

This idea was confirmed by the Tribunal in *Urbaser v Argentina*. The Tribunal while examining broad jurisdiction *ratione materiae* with broad *locus standi* concluded:

> [BIT] provision is completely neutral as to the identity of the claimant or respondent in an investment dispute arising "between the parties." It does not indicate that a State Party could not sue an investor in relation to a dispute concerning an investment.
>
> It further follows from the dual possibility to initiate an arbitration that the BIT does include in the dispute resolution mechanisms retained in Article X the hypothesis of a counterclaim, provided that the requirements defined by the provisions governing such mechanism are met.[114]

It appears, that tribunals will most probably admit counterclaims if IIA provides for state's *locus standi* and the scope of disputes arbitrable covers *all (any) dispute(s) concerning investment*.

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[109] Ibid.
[110] Argentina-Canada BIT (1991), Article 10(2). See also Hungary-Norway BIT (1991) and UK Model BIT (2008).
[111] Kjos, "The Scope of the Arbitration Agreement", 139
[112] USA-Estonia BIT (1994), Article 7(1).
[113] Lalive and Halonen, "On the Availability of Counterclaims", para. 7.20.
[114] *Urbaser v. Argentina*, paras.1143-1144. Worth noting, that in this case, again, the right to initiate arbitration was not analyzed separately from *ratione materiae*.

Therefore the *locus standi* factor cannot in itself solely play a decisive role in determining the presence or absence of consent to counterclaims. Rather it should be examined along with other factors, including jurisdiction *ratione materiae.*

To sum up on the Section 2.5, inasmuch as IIAs generally do not expressly provide for counterclaims the need for interpretation comes to the fore. The correct and effective interpretation of specific IIA provisions may determine how broad the consent is and whether that consent encompasses counterclaims. Broad or narrow formulation of *ratione materiae* and *locus standi* in combination may well assist a tribunal to conclude whether counterclaims are arbitrable or not.

2.6. How do different legal instruments deal with the consent requirement?

2.6.1. BIT as a primary source of consent

As discussed above in treaty-based arbitrations IIAs should serve as a primary basis for the determination of consent to counterclaims. This primacy emanates from the fact that IIA is a principal instrument via which the consent to arbitrate is proposed.

For example, in *Saluka v Czech Republic* the Tribunal stated that its "jurisdiction [was] *primarily* governed by Article 8 of [Netherlands-Czech and Slovak Republic BIT].[115] Apparently the Tribunal mentioned the word "*primarily*" to show the primacy of the BIT over UNCITRAL Arbitration Rules. Further it backed its statement by emphasizing that jurisdiction in principle over counterclaims should be determined by the Treaty.[116] Similarly, in *Oxus v Uzbekistan* the Tribunal ruled that the scope of jurisdiction of arbitral tribunal, including jurisdiction over counterclaims was defined by the state's offer to arbitrate given through the BIT.[117] In *Paushok v Uzbekistan* the Tribunal's first point to note was that its jurisdiction rests on the Treaty.[118]Another case where the Tribunal underlined the primacy of BIT was *Roussalis v Romania*. The Arbitral Tribunal while analyzing whether Romania's consent to arbitration encompassed counterclaims noted:

> [it] must be determined *in the first place* by reference to the dispute resolution clause contained in the BIT.[119]

[115] *Saluka v Czech Republic*, para. 21.
[116] Ibid. para. 37.
[117] *Oxus Gold plc v. Republic of Uzbekistan, the State Committee of Uzbekistan for Geology & Mineral Resources, and Navoi Mining & Metallurgical Kombinat*, UNCITRAL, Award, 17 December 2015, para. 945.
[118] *Paushok v Mongolia*, para. 685.
[119] *Roussalis v Romania*, para. 866.

All the cases above clearly demonstrate that consent that conditions the jurisdiction of a tribunal over counterclaims stems from IIA. The Tribunals in the cases above verified that IIA is a main instrument upon which the parties agree to arbitrate.

Consequently consent to counterclaims should be determined based on IIA. On the other side, IIA itself includes reference to other instruments. Subsection below analyzes how these instruments deal with consent to counterclaims.

2.6.2. Irrelevance of arbitration rules for the determination of consent

Subsubsection 2.6.1. stressed that IIA is a key instrument for the determination of consent to counterclaims and Section 2.5 explored how IIAs are supposed to be interpreted and which formulations in IIA are worth to pay attention to. Besides, IIAs contain reference to other tools, like UNCITRAL Arbitration Rules or SCC Arbitration Rules. Insofar as these tools are included into the dispute resolution clause of IIA proposed by a host state, then they are supposed to be considered as a part of consent.

If so the question may arise whether being a part of consent these instruments may play any role for the determination of consent and whether they may extend the scope of parties' consent so that to encompass counterclaims. The answer is negative. These instruments neither play any role for the determination of consent nor they in themselves may extend the jurisdiction of a tribunal. UNCITRAL Arbitration Rules and SCC Arbitration Rules serve only as a supplementary tool for the assertion of jurisdiction over counterclaims. They regulate the procedure of resolving of a dispute, not playing any role in defining the scope of consent. If they do not define the scope of consent, consequently they may not extend this scope as well. As Atanasova notes the "inclusion of counterclaims in the scope of the parties consent in investment treaty arbitration cannot be presumed only by the reference in the arbitration agreement to a particular set of arbitration rules".[120] Therefore despite being a part of consent, these tools may not in themselves enlarge the scope of consent so that to encompass counterclaims. The analysis below discovers how various arbitration rules deal with the issue of consent to counterclaim and why these instruments may not extend the scope of consent.

[120] Atanasova, Benoit and Ostřanský, "Counterclaims in ISDS", 12.

UNCITRAL Arbitration Rules

UNCITRAL Arbitration Rules expressly permit counterclaims. UNCITRAL (2010) Arbitration Rules state that

> The response to the notice of arbitration may also include:
> (e) A brief description of *counterclaims* or claims for the purpose of a set-off, if any, including where relevant, an indication of the amounts involved, and the relief or remedy sought[121],

thereby admitting that the respondent may submit the counterclaim. Further it provides that

> 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.[122]

The previous version of UNCITRAL Arbitration Rules, required that counterclaims arise only "out of the same contract".[123] There was a critique as to this wording, which was regarded as "inappropriate to arbitration arising under international treaties".[124] The application of UNCITRAL (1976) Arbitration Rules gains more complexity when investor-state arbitration takes place absent an investment contract between an investor and a host state. UNCITRAL's Working Group on Arbitration and Conciliation suggested, that the provision "be modified so as to allow counter-claims that were substantially connected to (or arose out of) the initial claim".[125] Eventually the version that had initially been regarded as "inappropriate" was adopted.

However, there is no express reference to consent to counterclaim in UNCITRAL Arbitration Rules. The reason is mainly that these rules were elaborated for commercial arbitration, wherein the right to counterclaim is generally accepted. The complexity of applying UNCITRAL Arbitration Rules in treaty-based investment arbitrations arises by reason of different mechanisms of reaching an agreement to arbitrate in treaty arbitration and commercial arbitration. In the former it is made through "arbitration without privity", in the latter via "arbitration with privity".[126]

In *Saluka* case decided under UNCITRAL Arbitration Rules 1976, interpreting the BIT provision, the Tribunal noted:

[121] UNCITRAL Arbitration Rules (as revised 2010), Article 4.
[122] Ibid, Article 21(3)
[123] UNCITRAL Arbitration Rules (1976), Article 19(3)
[124] Atanasova, Benoit and Ostřanský, "Counterclaims in ISDS", 10
[125] Ibid.
[126] See Section 2.2.

> [I]n principle, the jurisdiction conferred upon it by Article 8, particularly when read with Article 19.3, 19.4 and 21.3 of the UNCITRAL Rules, is in principle wide enough to encompass counterclaims.[127]

First of all, the statement *"jurisdiction conferred upon it by Article 8"* shows that the jurisdiction of the Tribunal over counterclaims is based on (Article 8 of) the BIT in question, but not on the arbitration rules. Moreover, word *"particularly"* in the Tribunal's analysis strengthens this notion. Hence, according to Tribunal's finding UNCITRAL Arbitration Rules are of no impact on the determination of the scope of consent. In *Paushok* case the Tribunal took the same approach.[128]

As for whether UNCITRAL may broaden the scope of consent so that to include counterclaims the answer is again negative. *Oxus v Uzbekistan* case may be an illustration. The BIT's dispute resolution clause included only disputes concerning the obligation of Uzbekistan under that BIT[129]. The Tribunal stated:

> As concerns Article 21(3) of the UNCITRAL Arbitration Rules, the Arbitral Tribunal does not consider that this provision creates a jurisdiction where there is none. All it does is stating that counter-claims are admissible and can be submitted to the extent that they already fall under the scope of jurisdiction of the Arbitral Tribunal.[130]

It follows from the Tribunals opinion that UNCITRAL Arbitration Rules do not in themselves create jurisdiction, and counterclaims would have been accepted only if they had been encompassed by the parties' consent. Therefore, despite the express permission of counterclaims, UNCITRAL does not affect the scope of consent so that to include counterclaims.

To sum up, the cases above demonstrate that UNCITRAL Arbitration Rules neither create consent nor they affect the scope of that consent.

SCC and ICC Arbitration Rules

In SCC and ICC Arbitration Rules regulation of the issue of counterclaims is almost the same as in UNCITRAL Arbitration Rules. SCC Arbitration Rules state that Respondent's Answer to the Claimant's request for arbitration shall include among others *"a preliminary statement of any counterclaims or set-off"*.[131] However, the issue of consent from SCC Arbitration Rules' position is obscure: there is no reference to the consent.

[127] *Saluka v Czech Republic*, para. 39
[128] *Paushok v Mongolia*, para. 689.
[129] UK-Uzbekistan BIT (1993), Article 8(1).
[130] *Oxus v Uzbekistan*, para. 944.
[131] SCC Arbitration Rules (2017), Article 9, SCC Arbitration Rules (2010), Article 5.

In *AMTO v Ukraine*, which was decided under SCC Rules (1999) the Claimant stressed that ECT did not permit the Respondent to advance a counterclaim. The Respondent in its turn stated that Article 21 of SCC Rules was applicable in that case thereby permitting counterclaims.[132] Tribunal noted:

> The jurisdiction of an Arbitral Tribunal over a State part counterclaim under an investment treaty depends upon *the terms of the dispute resolution provisions of the treaty*, the nature of the counterclaim, and the relationship of the counterclaims with the claims in the arbitration.[133]

Accordingly, the Tribunal emphasized the importance of the Treaty and dependence of admission of counterclaims mainly upon the offer of the state to arbitrate contained in that Treaty. Therefore, the Tribunal in fact gave priority to the Treaty provision over the arbitration rules in case of their conflict with regard to the consent to counterclaims.

Similarly to SCC Arbitration Rules, ICC Arbitration Rules provide that *"any counterclaims made by the respondent shall be submitted with the Answer"*.[134] ICC Arbitration Rules do not provide for the consent to counterclaims too. The reason is, as stated above, that these arbitration rules designed for commercial arbitration, where both parties to the dispute may submit claims. Even in case of dismissal of counterclaims in commercial arbitration, a respondent may submit its claims in new proceeding, this time acting as a claimant. So far there has been decided no treaty-based arbitration case under ICC Arbitration Rules, where the matter of counterclaims stood before a tribunal. Nevertheless, the approach the Tribunals took in *Saluka* and *AMTO* cases may serve as a benchmark for a scenario, when tribunals have to apply in treaty-based arbitration the arbitration rules oriented for commercial disputes.

To sum up, reference to UNCITRAL Arbitration Rules and SCC Arbitration Rules in IIAs is reference to the tools that regulate the procedure of dispute resolution and they do not extend the jurisdiction of tribunal over counterclaims.

2.6.3. Consent in the context of ICSID Convention

Inasmuch as ICSID Convention was elaborated especially for investor-state dispute settlement, the issue of consent therein is clear-cut. Article 25 of the Convention clearly demonstrates that consent plays a central role for the assertion of jurisdiction of a tribunal. However, ICSID does not *per se* serve as a primary instrument where the parties' consent to

[132] *Limited Liability Company AMTO v Urkaine*, SCC Case No. 080/2005 (ECT), Final Award, 26 March 2008, para 117.
[133] Ibid, para. 118
[134] ICC Arbitration Rules (2012), Article 5(5)

arbitration comes from. This finding emanates from its Preamble stating that "no Contracting State shall by the mere fact of its ratification, acceptance or approval of this Convention and without its consent be deemed to be under any obligation to submit any particular dispute to conciliation or arbitration".[135]

This idea is backed by the Report of Executive Directors on the ICSID Convention stressing that "[c]onsent may be given, for example, in a clause included in an investment agreement, providing for the submission to the Centre of future disputes".[136] Hence, the consent between a state and an investor on submission a dispute to arbitration is reached not through ICSID, but through other tools (in our case via IIA)

As regards particularly to counterclaims, ICSID Convention sets that

> [e]xcept 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.[137]

As mentioned above, ICSID itself is not a source of consent. Then it appears that by stating *"provided that they are within the scope of the consent of the parties"* ICSID refers tribunals to other sources (in our case to IIA). Based on that IIA tribunals will define whether scope of consent encompasses counterclaims or not. Therefore, tribunals should determine the scope of parties' consent outside ICSID, i.e. pursuant to the wording of IIA.

However, in *Roussalis v Romania* arbitrator Reisman was of another opinion stating that

> …when the States Parties to a BIT contingently consent, *inter alia*, to ICSID jurisdiction, the consent component of Article 46 of the Washington Convention is *ipso facto* imported into any ICSID arbitration which an investor then elects to pursue.[138]

Pursuant to Reisman's view, when Roussalis had initiated the proceedings against Romania, he impliedly gave his consent to counterclaims. Nevertheless, this notion deserves more critique than support. In *travaux préparatoires* of ICSID, Aron Broches stressed with respect to Article 46, that the jurisdiction of the Tribunal would not go beyond the consent of parties.[139] A state cannot contest, that the possibility of counterclaims is implied under that offer, unless the consent is not included into the offer to arbitrate. Romania's offer in that dispute, did not extend to counterclaims, consequently, the Claimant accepted the offer only within the terms proposed by the State, i.e. without the right to counterclaim.

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[135] ICSID Convention, Preamble.
[136] Report of the Executive Directors on ICSID Convention, para. 24.
[137] ICSID Convention, Article 46.
[138] *Roussalis v Romania*, W.Michael Resiman's Dissenting Opinion on date 28 November 2011.
[139] Jose Antonio Rivas, "ICSID Treaty Counterclaims: Case Law and Treaty Evolution", *Transnational Dispute Management* 1 (2014): 12.

Bravin claims that

> [t]here is support in the text of Article 46 for a default rule in favor of a finding of consent based on the investor's affirmative decision to file his claim with ICSID. Article 46 provides for the arbitration of closely related counterclaims "*[e]xcept as the parties otherwise agree*." Absent such a contrary agreement, the presumption is that counterclaims will be arbitrable.[140]

This notion reflects the approach of broad interpretation of Article 46. However, this Article should not be construed restrictively or broadly. As all the treaties, ICSID Convention is supposed to be "interpreted … with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose".[141] Moreover, Bravin's statement *"absent such a contrary agreement, the presumption is that counterclaims will be arbitrable"* makes the formulation *"within the scope of the consent"* meaningless. If to exclude this expression from the Article 46, we will have exactly the same meaning, what Bravin conveys to us:

> 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.

Accordingly, if parties do not agree otherwise, then the consent is deemed to be given. The modification made above precisely reflects the same idea, which Bravin stated. Under this notion, the phrase *"except as the parties otherwise agree"* serves as a determinant of the existence of consent, thereby making the formulation *"within the scope of the consent"* pointless. If ICSID drafters wanted to send us the idea shared by Bravin they would have probably excluded the phrase *"within the scope of the consent"* from the text of the Convention.

One should keep in mind that ICSID itself is not a source of consent. Hence, ICSID may not serve as a basis for tribunal's jurisdiction over counterclaims, this jurisdiction over may be asserted based on consent.

2.7. Conclusion

Consent to counterclaims remains one of the controversial issues, which tribunals face in treaty arbitration. Taking into account that arbitration as such rests upon the parties' agreement, the complexity of treaty-based investment arbitration stems mainly from the fact that parties do not reach this agreement directly. This process is called "arbitration without privity", where a state gives its offer (consent) to arbitrate through IIA and an investor accepts

[140] Bravin and Kaplan, "Arbitrating Closely Related Counterclaims", 7
[141] Vienna Convention on Law of the Treaties, Article 31.

this offer simply by instituting arbitral proceedings. Another peculiarity of treaty-based arbitration as opposed to commercial arbitration is that scope of parties' consent is not mutually agreed between a state and an investor. In fact, this scope is defined by a state through its consent (offer) given via IIA.

An investor in its turn may either accept this offer by initiating arbitration or reject it. An investor may not modify the scope of state's consent, because any modification will be tantamount to counter-offer to arbitrate.

To answer the question on whether respondent state's counterclaims are allowed, a tribunal has to define the scope of parties' consent, the borders of which are actually set by a state through IIA. In treaty arbitration the fate of counterclaims will depend upon whether those counterclaims are included into the state's offer to arbitrate to be accepted by an investor. Hence, if counterclaims come within the offer proposed by a state, investor's acceptance means the acceptance of possibility to raise counterclaims as well.

Inasmuch as consent to arbitrate is given via IIA the starting point for a tribunal's analysis must be IIA itself. It is the instrument through which the parties reach an agreement on arbitration, albeit indirectly. Rarely IIAs expressly provide for counterclaims. However, tribunals should not in their analysis be confined by the absence of explicit reference to counterclaims, as much as some formulations of treaty provisions may still indicate permissibility of counterclaims. Here comes into play an effective interpretation of IIA to be made in accordance with VCLT provisions. The scope of consent may only be determined through the correct interpretation, which will later on lead a tribunal to the conclusion on whether counterclaims are allowed or not.

BITs as a rule include reference to ICSID Convention, UNCITRAL or SCC Arbitration Rules. Despite being a part of consent, these instruments do not extend the scope that consent so that to cover counterclaims. The cases analyzed above show that the scope of consent may only be determined within the borders set in IIA through the right interpretation of that IIA and no other instrument may extend this scope.

III. CONNECTEDNESS OF COUNTERCLAIMS WITH THE PRIMARY CLAIM

Chapter 2 explored consent to counterclaims as a jurisdictional requirement. However, consent is not the only element necessary for the admission of counterclaims. Another requirement which is no less important for counterclaims to be heard by a tribunal is connectedness of counterclaims with a primary claim. One of the early disputes, where the Court mentioned the requirement of connectedness was *Chorzow factory* case.[142] In that case, the Court observed, that

> the counter-claim [was] based on Article 256 of the Versailles Treaty, which article [was] the basis of the objection raised by the Respondent, and that, consequently, it [was] juridically connected with the principal claim.[143]

Adjudicative bodies refer to this requirement actually in each system that provides for counterclaims.[144] The reason is apparent: the rationale for permission of counterclaims, i.e. procedural economy and the better administration of justice may only be substantiated by the connexity requirement.[145]

The requirement of close connection between a primary claim and a counterclaim is not the issue that regulated only by international instruments. Many states fixed the connexity requirement in their municipal law.[146] This in its turn proves that the close connection requirement in legal disputes became a well-established principle, and arbitration is not an exception.

In treaty-based investment disputes, connexity requirement may be provided in IIAs[147] or other legal instruments[148] applicable to a dispute. In such a case tribunals will apply this requirement as a mandatory provision. However there may be a scenario when there is no reference to connectedness requirement in legal instrument(s) applicable to a dispute. In such a scenario a tribunal will in all likelihood apply close connection requirement as a principle.

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[142] Atanasova, Benoit and Ostřanský, "Counterclaims in ISDS", 26.
[143] *Case concerning the Factory at Chorzow (Germany v. Poland),* Claim for Indemnity, Merits, Judgment of 13 September 1928, PCIJ Series A, No. 17 (1928) p.38, para.1.
[144] ICSID Convention, Artice 46; Rules of the International Court of Justice, Art 80. Other international dispute settlement bodies have held that the close connection requirement is an ubiquitous part of general principles of law of procedure, e.g. *Westinghouse Electric Corp v Islamic Republic of Iran* Case No. 389, 12 Feb 1987, Award 6 Iran-US CTR II (1984) at 1; UNCITRAL Arbitration Rules 2010, Art 21(3).
[145] Kjos, "The Scope of the Arbitration Agreement", 147
[146] See for example, Norwegian Dispute Act, Swedish Code of Judicial Procedure (1942), Civil Procedure Code of the Russian Federation (2002), Civil Procedure Code of Azerbaijan Republic (1999).
[147] See for example TPP Agreement.
[148] See for example ICSID Convesntion or UNCITRAL Arbitration Rules (1976).

This Chapter focuses on the requirement of close connection of counterclaims with primary claims. Before going deep into the discussion of this requirement, the matter that should be started with is that the connectedness requirement relates to admissibility issues.

3.1. Connectedness as an admissibility issue.

Unlike consent, which is purely jurisdictional issue, the connexity requirement conditions the admissibility of counterclaims. ICJ Rules of Court in Article 80 delineates jurisdiction from connectedness[149], thereby implying that connectedness does not pertain to jurisdictional matters. Consequently, under ICJ Rules connexity requirement relates to admissibility issues.

Lalive analyzing the connectedness requirement of counterclaims in Article 46 of the ICSID Convention stresses that this requirement is additional to the jurisdictional requirements in Article 25 and thus pertains to the admissibility of such counterclaims.[150] Likewise, Kjos stresses that similarly to "forum election agreements, connexity is a question of admissibility rather than jurisdiction".[151]

In practice though the distinction between admissibility and jurisdiction is not clear. This mainly stems from the fact that tribunals while considering counterclaims do not delineate the borderline between jurisdiction and admissibility, thereby discussing both consent and connectedness in one phase, jurisdictional.[152]

Nevertheless there are few treaty-based investment cases, where tribunals expressly stressed that requisite connection serves the admissibility purposes. So, the Tribunal in *Metal-Tech v Uzbekistan* noted as regards to Article 46 of ICSID Convention:

> [T]he second [connectedness] requirement supposes a connection between the claims and the counterclaims. It is generally deemed an admissibility and not a jurisdictional requirement.[153]

Another case where connectedness was attributed to admissibility was *Oxus v Uzbekistan*. The Tribunal noted that

> a sufficient "*close connection*" or "*nexus*" exist[ed] between Claimant's claims and Respondent's counter-claims to justify the admissibility of Respondent's counter-claims.[154]

[149] Rules of the Court of International Court of Justice, Article 80.
[150] Lalive and Halonen, "On the Availability of Counterclaims", para. 7.10.
[151] Kjos, "The Scope of the Arbitration Agreement", 147
[152] See for example *Saluka v Czech Republic,* and *Paushok v Mongolia*
[153] *Metal-Tech v Uzbekistan*, para. 407.
[154] *Oxus v Uzbekistan*, para. 940.

Likewise, in *Goetz v Burundi* the Tribunal considered this condition as an issue of admissibility.[155]

Therefore, if jurisdiction over counterclaims, exercised by means of consent, reflects whether a tribunal may hear any counterclaim at all, admissibility presumes whether a particular counterclaim closely connected with a primary claim.

3.2. How do legal instruments approach connectedness requirement?

The way as to how the connexity requirement is regulated by various legal instruments is not uniform at all.

ICSID Convention requires that counterclaims arise "directly out of the subject-matter of the dispute".[156] The requirement of Article 46 should be discerned from that of Article 25(1) - "arising directly out of an investment".[157] The former requires a close connection with the subject-matter of the dispute and relates to the issue of admissibility, whereas, the latter requires a close connection with an investment and concerns to the jurisdictional matters.[158] Schreuer is also of opinion that close connection required by Art. 46 is not a matter of jurisdiction, reasoning that the wording of that provision makes it clear that "arising directly" requirement must be fulfilled in addition to the jurisdictional requirements.[159]

According to Lalive's view the difference between "subject-matter" in Article 46 and "investment" in Article 25 is not immediately clear:

> The same subject-matter is probably something different – and *narrower* – than the same investment as that term is used in Article 25 of the ICSID Convention (a "dispute arising directly out of an investment"). If it were not, there would have been no reason to add the word "*subject-matter*" to Article 46, since the question of "*jurisdiction*" would in any event have covered the issue.[160]

There is no reason not to agree with this statement, as long as by adding "*provided that they are …within the jurisdiction of the Centre"*, the drafters of ICSID thereby convey to us that *"subject-matter"* and *"jurisdiction"* in Article 46 are definitely two distinct categories.

UNCITRAL Arbitration Rules of 1976 envisage, that *"*the respondent may make a counter-claim arising out of the same contract or rely on a claim *arising out of the same*

[155]Dafina Atanasova, Adrián Martínez Benoit, Josef Ostřanský, "The Legal Framework for Counterclaims in Investment Treaty Arbitration", *Journal of International Arbitration* 31, No. 3 (2014): 378.
[156] ICSID Convention, Article 46 and ICSID Arbitration Rules, Article 40
[157] Steingruber, "Comments on Goetz v Burundi case", 299.
[158] Ibid. See also Anne Hoffmann, "Counterclaims in Investment Arbitration", *ICSID Review* (2013): 5, doi:10.1093/icsidreview/sit032
[159] Christoph Schreuer, *The ICSID Convention: A Commentary 2nd ed* (Cambridge University Press, 2009): 751
[160] Lalive and Halonen, "On the Availability of Counterclaims", paras. 7.11-7.12.

*contract fo*r the purpose of a set-off."[161] Worth to note that such wording of connexity requirement provided in Article 19(3) is incompatible with treaty arbitration. Frequently, investors invoke IIA's arbitration clause to initiate proceedings against a state absent any investment contract with that state. It appears that if the investor chooses UNCITRAL Arbitration Rule 1976, then the state is deprived of the right to counterclaim when there is no investment contract with that investor.

In the light of treaty-based investment arbitration it is, therefore, preferable to interpret the term "contract" as a source of the right constituting the object of the claim, i.e. as "investment".[162] Taking into consideration this factor the Tribunal in *Saluka case* did not confine the connexity requirement only to the "same contract" stating that

> [i]n 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 connexion with the primary claim to which it is a response.[163]

The Tribunal thereby confirmed that the formulation *"same contract"* should not be interpreted in its strict sense in treaty-based investment arbitrations.

Unlike its predecessor UNCITRAL Arbitration Rules 2010 provide that

> [t]he 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.[164]

The new version of UNCITRAL Arbitration Rules does not provide for close connection requirement. The wording above was recognized as "broad enough to encompass a wide range of circumstances and did not require substantive definitions of the notions of claims for set-off and counterclaims".[165] Apparently, one of the reasons for this amendment was to overcome the complexity that the previous formulation created for treaty-based arbitration. Moreover, absent an express reference to connectedness, it is argued that tribunals might apply it as a general principle of procedure.[166]

As stated above IIAs rarely contain provision on counterclaims, consequently no reference to close connection requirement can be found. Nevertheless, few exception there do exist. One of these exceptions is a new generation investment treaty, namely TPP. This Treaty goes even further, by not only permitting counterclaims, but also requiring that

[161] UNCITRAL Arbitration Rules 1976, Article 19(3).
[162] Douglas, *The International Law of Investment Claims,* para. 494.
[163] S*aluka v Czech Republic*, para. 61.
[164] UNCITRAL Arbitration Rules 2010, Article 21(3).
[165] United Nation Commission on International Trade Law, *Report of the Working Group on Arbitration and Conciliation on the Work of its fiftieth session*, New York, 9-13 February 2007, para. 31.
[166] David Caron, Lee Caplan and Matti Pellonpää, *The UNCITRAL Arbitration Rules: A Commentary*, (Cambridge University Press, 2006): 414.

counterclaims be in connection with the *factual* and *legal* basis of the claim.[167] Next Section analyzes what factual and legal connexity imply.

COMESA Investment Agreement provides that counterclaims may be asserted not only due to violation of obligations by the investor, but also by virtue of the violations of obligations under the domestic law.[168] In spite of the absence of express mention to connectedness, COMESA impliedly extends the connexity requirement to the violation of domestic law as well. This approach though is not uniformly accepted by arbitral tribunals.

To summarize, the instruments above approach the connectedness requirement differently, which consequently leads to the non-uniform application of this requirement in investment disputes.

3.3. What does the connectedness requirement imply?

Indeed, there are not exact criteria as to the assessment of connectedness. As the Tribunal in *Saluka case* stressed:

> The nature and extent of the necessary close connection may be variously expressed. No single attempt to define this requirement with universal effect is likely to be satisfactory, since so much will always turn on the particular circumstances of individual cases, including not only their facts but also the relevant treaty and other texts.[169]

This is mainly due to the reason that circumstances vary from case to case.

This requirement was previously endorsed in ICJ case. So, in *Armed Activities case* the Tribunal emphasized that

> as a general rule … the direct connection between the [counter-claim and the principal claim] must be assessed both in fact and in law.[170]

But the Court did not further clarify what *"connection in fact and in law"* meant.

Douglas clarifies this formulation in the context of investment arbitration through two possible interpretations of connexity requirement:

(i) narrow interpretation – implying that the legal instrument of primary claim and counterclaim coincide (juridical connexity) and

(ii) broad interpretation - where delineating principle might be the object of the primary claim, which is the investment, so that any counterclaims relating to the investment

[167] Trans Pacific Partnership Agreement (2016), Article 9.19(2).
[168] Investment Agreement for the COMESA Common Investment Area (2007), Article 28(9).
[169] S*aluka v Czech Republic*, para. 63.
[170] *Case Concerning Armed Activities on the Territory of the Congo (Democratic Republic of the Congo v Uganda)*, Counter-Claims Order, 29 November 2001, ICJ Rep. 660, para. 36.

would be within the tribunal's jurisdiction *ratione materiae*, whatever their legal source (factual connexity).[171]

Accordingly, juridical connection means, that claims and counterclaims must have the same legal grounds whereas factual connectedness "is based on the premise that the scope of connection should be delineated by the object of the primary claim - the underlying investment".[172] Juridical connectedness must be interpreted by the reference to the same legal instrument that governs the rights and obligations of both the state and investor.[173]

When it comes to investment arbitration cases, the Tribunal in *Urbaser v Argentina* analyzed both factual and juridical connexity of counterclaims advanced by Argentina. The dispute arose out of the agreement on concession for water and sewage services.[174] Argentina counterclaimed for the alleged failure by Urbaser to provide the necessary investment thereby violating its obligations based on human right to water.[175] The Tribunal noted that

> [t]he factual link between the two claims [was] manifest. Both the principal claim and the claim opposed to it [were] 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.[176]

Further it noted that

> [t]he legal connection [was] also established to the extent the Counterclaim [was] not alleged as a matter based on domestic law only. Respondent [argued] indeed that Claimants' failure to provide the necessary investments [had] caused a violation of the fundamental right for access to water, which was the very purpose of the investment agreed upon in the Regulatory Framework and the Concession Contract and embodied in the protection scheme of the BIT.[177]

According Tribunal's view, the factual link sufficed to admit counterclaims, albeit the juridical connexity was also determined.

In *Oxus v Uzbekistan* the Respondent based its counterclaims on double premise: factual basis and legal basis.[178] In fact, the Uzbekistan's counterclaims might be divided into three groups:

(i) Claims for general misconduct by Claimant;

(ii) Claims arising out of the sale of silver and

(iii) Claims under the Special Dividend Agreement ("SDA").[179]

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[171] Douglas, *The International Law of Investment Claims*, para. 489.
[172]Jacek Kozikowski, "Counterclaims in Investment Arbitration: Boosting a Host State's Position in Environmental Disputes with Foreign Investors (Draft Paper)", 11-12, http://www.academia.edu/
[173] Kjos, "The Scope of the Arbitration Agreement", 149.
[174] *Urbaser v. Argentina*, paras. 34-37.
[175] Ibid., para. 36.
[176] Ibid., para. 1151.
[177] Ibid.
[178] *Oxus v Uzbekistan*, para. 937.

The Tribunal in its turn analyzed the factual connexity in the first and second type of counterclaims, and juridical connection as regards to the third group of counterclaims.[180] In relation to misconduct and silver sale counterclaims, the Tribunal was not convinced that there was the necessary close connection by reason

> that the underlying factual matrix refer[ed] largely to the way in which AGF[181] operated, not to the circumstances in which Claimant invested into AGF.[182]

As concerns the SDA counterclaims, the Tribunal did not deny that they rested on the same legal instrument as the primary claim, but had to dismiss them due to the reason that SDA contained different forum selection and choice of law clause.[183] Ultimately all the counterclaims asserted by Uzbekistan were dismissed.[184]

The approach the Tribunal took in this case is more flexible and adaptive to treaty arbitration. The Tribunal probably realized that counterclaims relating to general misconduct and silver sale could not anyhow have been based on the same legal instrument with the primary claim, and consequently examined only factual connection.

Frequently, host states finding no ground to base counterclaims on, refer to the alleged violation of their public law committed by investors. This takes place mainly by virtue of non-inclusion of investors' obligations into IIAs. Moreover, the absence of investment contract or any other instrument directly relating to investment (concession, license etc.) leaves no other choice for a state but to base its counterclaims merely on the violation of municipal law. This might seem quite reasonable insofar as host state's law remains the only source where the investor's obligations emanate from, however tribunals oftentimes do not accept such counterclaims.

In *Saluka v Czech Republic* the Respondent submitted two types of counterclaims: (i) arising out of violation of Share Purchase Agreement ("SPA") and (ii) those concerning the violation of general domestic law.[185] The Tribunal considered the issue of close connection only as regards to the second type of counterclaims. In its analysis, the Tribunal referred to various previous cases, albeit they rested on the terms of instruments, which differed from those of Article 8 of the Treaty in question.[186] It concluded, that the cases it addressed to, nevertheless, reflected a general legal principle with respect to the nature of close connection

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[179] Ibid., para 935.
[180] Ibid., paras. 955-958
[181] Amantaytau Goldfields AO, the subsidiary of the Claimant.
[182] *Oxus v Uzbekistan*, para. 956.
[183] Ibid., para. 957.
[184] Ibid., para. 959.
[185] *Saluka v Czech Republic*, paras. 48 and 59
[186] Ibid, para.76

and that disputants in their written and oral submissions had not said, that Czech law did not accept that general principle.[187] Ultimately, Tribunal ruled, that

> it is apparent that those heads of counterclaim involve non-compliance with the general law of the Czech Republic.
> Taken at face value, and on the basis of their own terms as pleaded by the Respondent… counterclaim cannot be regarded as constituting …"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.[188]

According to Tribunals position, the counterclaims for the violation of domestic law could not be interpreted as constituting "indivisible whole" with the primary claim, thus were rejected.

As for the counterclaims, which rested on the violation of the Share Purchase Agreement, the Tribunal while considering them, expressed its concerns with regard to (i) the element of consent and (ii) the identity of parties to that Agreement. However it omitted the issue of close connection what might lead to the conclusion, that the counterclaims complied with this connexity requirement. Apparently if the Tribunal was not satisfied with the connectedness requirement in counterclaims for breach of SPA, it would have emphasized this matter. Eventually, the Tribunal dismissed these counterclaims, as the SPA contained different dispute resolution clause.[189]

Scholars admitted this decision with certain degree of criticism, recognizing it as too demanding.[190] According to Lalive's view a close factual connection should suffice for counterclaims to be admissible:

> Whereas the investor might well have committed unlawful acts that are closely connected to the measures taken by the state that allegedly violate the BIT, it is hard to see a scenario where they may arise under the same legal order, namely international law.[191]

Atanasova is of opinion that if the consent given through BIT is broad enough to encompass the host state's counterclaims, "it is not necessary for the legal basis on which the counterclaim is brought to be the same as the one for the main claim in order to fall under the jurisdictional powers of the constituted tribunal."[192] Kjos supports this idea stressing that absent judicial connection a strong factual connexity could weigh in favor of the admissibility, since this serves procedural economy and the better administration of justice.[193]

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[187] Ibid.
[188] Ibid, paras. 78-79
[189] Ibid. paras. 52-58
[190] Lalive and Halonen, "On the Availability of Counterclaims", paras. 7.40-7.41.
[191] Ibid.
[192] Atanasova, Benoit and Ostřanský, "The Legal Framework for Counterclaims", 372.
[193] Kjos, "The Scope of the Arbitration Agreement", 154.

These opinions are reasonable enough mainly due to the fact that absent any obligations of investors under BIT, the juridical connexity in treaty arbitration seems almost infeasible.

Another case, where the Respondent based its counterclaims on the violation of domestic law was *Paushok v Mongolia* case. Considering the counterclaims, the Tribunal questioned, whether a State can "nonetheless invoke counterclaims, when an investor decides to initiate an arbitration under a bilateral investment treaty, even if that treaty contains no specific provision about counterclaims".[194] Taking into account, that it was satisfied with the consent requirement, Tribunal thoroughly examined the issue of close connection of counterclaims with the primary claim. Reviewing counterclaims it came to the conclusion, that they arose out of alleged violation of Mongolian public law, including tax laws, Mongolian legislation and regulations and by no means related to the investment.[195] Tribunal backed this point by stating that

> Indeed, through the Counterclaims the Respondent seeks to extend the extraterritorial application and enforcement of its public laws, and in particular its tax laws, to individuals or entities not subject to and not having accepted to submit to Mongolian public law or its courts. Thus, if the Arbitral Tribunal extended its jurisdiction to the Counterclaims, it would be acquiescing to a possible exorbitant extension of Mongolia's legislative jurisdiction without any legal basis under international law to do so…[196]

In *Paushok v Mongolia* the Tribunal took the same approach as in *Saluka v Czech Republic*, thereby stressing that violation of host state's public law remains out of jurisdiction of arbitral tribunal. The Tribunal's dismissal of the counterclaims due to the lack of close connection factor might seem reasonable insofar as the alleged violations of domestic law provisions were the only grounds, on which the Respondent based its counterclaims.

Yet arbitral tribunals' attitude towards tax issues is not uniform. In *Amco v Indonesia*, the Tribunal noted that there was no *a priori* rule or principle that might serve to remove tax claims from the jurisdiction of an ICSID tribunal.[197] In *Harris International Telecommunications, Inc v Iran* the Tribunal made distinction between income tax and withholding tax. According to Tribunals reasoning, a counterclaim for withholding tax if it remained unpaid, was under the Tribunals competence as long as it arose out of the relevant contract. This notion though deserves critique. The question that arises is: what is the source of these obligations? As a matter of principle it is the law, but not the contract where the

[194] *Paushok v Mongolia,* para. 687.
[195] Ibid, paras. 694-696
[196] Ibid. para. 695.
[197] Zachariy Douglas, "The enforcement of environmental norms in investment treaty arbitration", in *Harnessing Foreign Investment to Promote Environmental Protection*, eds. Pierre-Marie Dupuy and Jorge E. Viñuales, (Cambridge University Press, 2013): 432

obligations stem from.[198] The investor bears these obligations regardless of their specification in the investment contract. In *Amco v Indonesia*, the Tribunal stressed the necessity for distinction between the rights and obligations applicable to persons who are within the jurisdiction of host state; and right and obligations are applied to an investor as consequence of investment agreement.[199]

Another scenario is when the obligation to obey to host state's law is included into IIA. For example, COMESA Investment Agreement provides that "investors and their investments shall comply with all applicable domestic measures of the Member State in which their investment is made."[200] Does it cardinally differ from Aldrich's position noted above?[201] The answer seems more "yes" than "no". Well, in *Al Warraq v Indonesia* the Tribunal stated that

> [a]n investor of course has a general obligation to obey the law of the host state, but Article 9 raises this obligation from the plane of domestic law (and jurisdiction of domestic tribunals) to a treaty obligation binding on the investor in an investor state arbitration.[202]

As per the Tribunal's opinion, the internationalization of enforcement of domestic law resembles an umbrella clause that elevates the contractual claims to the treaty plane[203] and may well be accepted.

To sum up, to answer the question on what requisite connection implies requires a complex analysis. In fact there is not a uniform answer as to what is understood under the connectedness requirement: judicial or factual connexity; and whether enforcement of host state's public law falls under connectedness requirement as well. Inclusion of investors' obligations into IIA may speak in favor of admissibility of counterclaims asserted for violation of municipal law. If to apply connexity requirement strictly in treaty arbitration, there will be no room for the availability of any counterclaim at all.

3.4. Connectedness, but only after the consent

The fact that consent and connectedness relate to two distinct categories has already been discovered in this Thesis. One may question which of these two concepts has a priority over another? Actually, the consent has, but only in terms of order of consideration by a tribunal. This Section will prove that analysis of connexity comes only if a tribunal is satisfied

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[198] George Aldrich, *The Jurisprudence of the Iran-United States Claims Tribunal* (Oxford University Press, 1996): 116

[199] *Amco Asia Corporation and others v The Republic of Indonesia*, Resubmitted Case, ICSID Case No. ARB/81/1, Decision on Jurisdiction, 10 May 1988, 1 ICSID Reports (1993), para. 125.

[200] Investment Agreement for the COMESA Common Investment Area (2007), Article 13.

[201] See n. 200.

[202] *Hesham Talaat M. Al Warraq v. Republic of Indonesia*, UNCITRAL (1976), Final Award, 15 December 2014, para. 663.

[203] Ibid.

with a consent requirement. To put in another way, tribunals review factual or legal connexity of counterclaims with a primary claim, only after being ensured that those counterclaims are *a priori* permitted by the parties' consent.

In *Roussalis v Romania*, the host state's counterclaims were based on the violation of obligations under Privatization Agreement to invest additional 1.4 mln USD.[204] As seen, the investor's obligation directly related to the investment itself. Therefore the factual nexus between the counterclaim and the primary claim was apparent. However, absent jurisdiction over counterclaims due to lack of consent the Tribunal did not further examine close connection requirement.

In *Hamester v Ghana*, the Tribunal did not address the issue of close connection as well. In fact, the Respondent based its counterclaims on the fraudulent conduct and breach of fiduciary duty in connection with the initiation of and performance under the Joint Venture Agreement, which was concluded between Cocobod and the investor.[205] Ghana itself was not a party to the JVA. However, the Respondent counterclaimed for the losses incurred by the Cocobod.[206] Taking into consideration that Cocobod was neither party to the arbitration nor an organ of the State, Tribunal ruled that it had no jurisdiction over the counterclaims.[207] Despite the non-admission of the counterclaims due to the grounds stated above, the requirement of close connection was nevertheless met, as long as counterclaims arose out of investment. Hence, lack of jurisdiction leaded to the skipping of examination of connexity issues.

The Tribunal in *Metal-Tech v Uzbekistan* did not further analyze the connectedness requirement after finding no jurisdiction over counterclaims. It concluded:

> It follows from the foregoing discussion that the first requirement set in Article 46 of the ICSID Convention which relates to jurisdiction, including consent, is not met. As a consequence of its having no jurisdiction over the claims, this Tribunal has no jurisdiction over the counterclaims. It will thus abstain from reviewing whether the counterclaims meet the second requirement of Article 46 dealing with admissibility and demanding a connection with the claims.[208]

Lack of consent sufficed for the Tribunal not to review connectedness requirement.

Similarly, in *Rusoro v. Venezuela* lack of consent to counterclaims sufficed for the Tribunal to omit the connectedness requirement.[209]

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[204] *Roussalis v Romania*, para. 806.
[205] *Hamester v Ghana*, para. 356.
[206] Ibid.
[207] Ibid.
[208] *Metal-Tech v Uzbekistan*, para. 413.
[209] *Rusoro v. Venezuela*, paras. 629-633.

In *Paushok v Mongolia* after finding the wording of the BIT in question too broad to permit counterclaims, the Tribunal switched to the examination of connexity requirement.[210] Likewise, in *Saluka v Czech Republic* the Tribunal started the analysis of connectedness requirement after being satisfied that the consent requirement was fulfilled.[211]

All the cases above clearly illustrate that facing counterclaims in treaty arbitration, the starting point for tribunals should be the very consent, which determines whether counterclaims are arbitrable at all or not. Only in case of affirmative answer, arbitrators shall focus on the requisite connection of counterclaims with a primary claim. So far, no tribunal in treaty-based investment cases examined counterclaims by starting with the close connection requirement.

3.5. Consent and connectedness: necessity for distinction in the context of jurisdiction v. admissibility

The priority of consent over connectedness discussed above is not the only reason that causes the necessity for their distinction. This Section will explore the reasons for distinction of consent from connexity in the context of jurisdiction and admissibility.

At first glance this presents a pure theoretical problem. However, it is not so. Then the question may arise as to what is the practical importance of delineating of these two categories? Probably the best answer to this question might be the case brought by Jan Paulsson, where the Swiss court annulled the arbitral tribunal's decision.[212] According to the author's opinion

> [t]he fundamental error of the annulment was rather that it misunderstood the nature of the challenged arbitral decision. The Arbitrators made a decision as to the admissibility. The parties had agreed that all disputes under their contract would be decided by this particular tribunal, and as noted the validity of the arbitration clause was not at issue.[213]

The jurisdictional decisions are reviewable, but not others.[214] Consequently, the court may not annul the decision made with the violation of admissibility requirements by the arbitral tribunal. Paulsson notes that "[m]istakenly classifying issues of admissibility as jurisdictional may therefore result in an unjustified extension of the scope for challenging awards, and frustrate the parties' expectation that their dispute be decided by the chosen neutral tribunal."[215] Therefore, since connectedness requirement relates to admissibility, then

[210] *Paushok v Mongolia,* paras. 684-699
[211] *Saluka v Czech Republic*, paras. 37-39
[212] Jan Paulsson, "Jurisdiction and Admissibility", *Global Reflections on International Law, Commerce and Dispute Resolution* - Liber Amicorum in honour of Robert Briner (ICC Publication 2005): 601
[213] Ibid, p. 602
[214] Ibid.
[215] Ibid, p. 601.

tribunal's misinterpretation of this requirement with a subsequent erroneous ruling on this matter is non-reviewable. On the contrary, if the tribunal makes wrong decision as regards to the issue of consent to counterclaim, then the tribunal's decision may be reviewed.

Speaking about the challenge, worth to distinguish between ICSID and non-ICSID cases. Awards rendered in non-ICSID cases may be reviewed by the courts of the seat of arbitration or the courts of the place of enforcement of the award.[216] As for the awards rendered under ICSID, they are only reviewable before the *ad hoc* Committee pursuant to Article 52 of the ICSID Convention.[217]

The necessity for distinction of jurisdiction from admissibility is not limited only to the possible challenge of the award. Waibel outlines other consequences of this distinction that may have practical significance.[218] First of all, it is the date of request for arbitration (seisin). New facts that arise after that crucial date cannot be taken into consideration "for the purposes of assessing the tribunal's jurisdiction".[219] On the contrary, "new developments that concern admissibility may be taken into account".[220] Secondly, if the claim misses any jurisdictional requirement the tribunal will dismiss that claim, however, if the claimant fails to meet admissibility requirements, the tribunal may suspend the case in order to give the claimant the second chance to satisfy those admissibility requirements.[221]

Hence, the distinction of jurisdiction from admissibility is not just a theoretical issue, it bears great significance for practice as well. Misinterpretation of the consent requirement as an admissibility issue or connectedness as a jurisdictional matter will affect the right of parties to challenge an award.

3.6. Conclusion

The connectedness requirement being an admissibility matter has no less importance than consent. Even if there is consent to counterclaim, the lack of connection between a primary and a counterclaim will lead to dismissal of that counterclaim. However worth to note that consent and connectedness relate to two different categories jurisdiction and admissibility, respectively and the distinction between them should definitely be made

[216] Laurent Gouiffès and Melissa Ordonez, "Jurisdiction and admissibility: are we any closer to a line in the sand?", *Arbitration International* 31 (1) (2015): 119.
[217] Ibid.
[218] Michael Waibel, "Investment Arbitration: Jurisdiction and Admissibility", (University of Cambridge Faculty of Law Research Paper No. 9/2014, January 31, 2014):67, http://dx.doi.org/10.2139/ssrn.2391789
[219] Ibid.
[220] Ibid.
[221] Ibid.

inasmuch as this distinction reflects on the possibility to challenge an award. Jurisdictional issues may be reviewed, but admissibility ones not.

There are two possible interpretations of connectedness requirement: broad and narrow. The first one (factual connexity) implies that counterclaims should relate to investment and nothing more. The second one (juridical connexity) on the contrary, requires that counterclaims be based exactly in the same legal instrument as a primary claim. The complexity around juridical connectedness in treaty-based investment arbitrations arises due to the fact that IIAs commonly do not include investor's obligations. In such a scenario (absent any investment contract with a host state) host state's domestic law remains the only instrument on which investor's obligations are based on. However invocation of violation of municipal law provisions as a basis for counterclaims is not uniformly accepted by international arbitral tribunals.[222] This occurs due to the fact that tribunals do not always enforce domestic law extraterritorially in international investment arbitration. Therefore, the requirement that both primary claim and a counterclaim be based on the same legal instrument will in all likelihood exclude any counterclaim in treaty-based investment arbitration.

[222] See *Saluka* case and *Paushok* case

IV. FINAL CONCLUSION

From the analysis above it is clear that for counterclaims to be accepted by a tribunal consent and connectedness requirements should be met. These requirements should be distinguished from one another not just for theoretical reasons but for practical purposes as well.

Being a key element for asserting jurisdiction over counterclaims consent therefore relates to jurisdictional issues. By contrast to contract-based investment arbitration in treaty-based investment arbitration consent on arbitration is not reached directly. It operates as a two-step process that includes the host state's offer to arbitrate and investor's further acceptance of that offer. This process is called "arbitration without privity" which means that an investor and a state do not come into direct contact to reach an agreement on arbitration.

As a first step to reach consent a state proposes its offer to arbitrate via IIA. To start arbitration against a host state an investor must accept that offer. Generally IIAs do include any special requirement as to the expression of investor's acceptance. Absent any such requirement the initiation of arbitral proceeding suffices for the offer to be deemed accepted. Sometimes however IIAs require that an investor give a notice before submitting a case to arbitration. When an investor starts proceeding the consent on arbitration is reached.

Consent to arbitration does not necessarily extend jurisdiction of a tribunal over counterclaims as well. In order to be in tribunal's jurisdiction counterclaims should fall within the scope of parties' consent. The uniqueness of treaty-based investment arbitration is that the scope consent is not mutually agreed. The border of consent is confined to the offer made by a state via IIA. An investor in its turn may either accept or reject that offer, but may not modify it. Therefore the possibility of counterclaims in treaty-based investment arbitration will depend upon whether those counterclaims are included into the state's offer to arbitrate proposed through IIA.

Unfortunately, rarely IIAs expressly provide for counterclaims. However the absence of express reference to counterclaims does not necessarily infer that counterclaims are out of tribunal's jurisdiction. Therefore a very important task lays on a tribunal. The correct interpretation made by a tribunal may detect the possibility of counterclaims even if IIA is silent on counterclaims.

As long as IIA is a tool via which the consent is reached, then it should be a primary source where a tribunal must refer while determining the possibility of counterclaims. IIA often include reference to other instruments like UNCITRAL Arbitration Rules or SCC Arbitration Rules. Provisions of those instruments do not always correspond to IIA provision

as concerns to possibility of counterclaims. Where IIA does not allow counterclaims, those counterclaims will be out of tribunal's jurisdiction and supplementary instruments mentioned above may not tribunal's jurisdiction so that to include counterclaims.

The second requirement to be fulfilled for counterclaims to be admitted is connectedness. This requirement infers that a counterclaim must have close connection with a primary claim. Unlike consent requirement which is a jurisdictional matter, the connexity requirement conditions the admissibility of counterclaims and hence relates to admissibility matters.

Unfortunately, connectedness requirement is not uniformly regulated by legal instruments that applied in investment arbitration. Some of them require that counterclaims arise *"directly out of the subject-matter of the dispute"*[223], others require that they arise *"out of the same contract"*[224], third specify that counterclaims must be *"in connection with the factual and legal basis of the claim"*.[225] Divergent regulation of connectedness requirement leads to non-uniform application of it.

Moreover, there is no exact answer as to what close connection requirement implies. There are two approaches: first one means that counterclaims must rest on the same legal instrument as a primary claim (juridical connexity) and second one purports that counterclaims are admissible if they arise out of investment (factual connexity). Absent investors' obligations in IIA, the juridical connexity makes admission of counterclaims almost impossible in treaty-based investment arbitration.

Despite the fact both consent and connectedness requirements are equally important for admission of counterclaims, consent requirement should come first in the order of tribunal's analysis. Tribunals analyze admissibility matters only after being satisfied with jurisdictional requirements. Therefore if consent requirement is not met, a tribunal will dismiss counterclaims without further analysis of connectedness requirement.

Moreover the distinction of consent requirement from connectedness in the light jurisdiction v. admissibility bears practical importance. Jurisdictional decisions may further be challenged, but decisions on admissibility - not. Therefore attribution of consent requirement to admissibility and connexity to jurisdiction will have adverse effect on the right of the parties to challenge the award.

[223] ICSID Convention, Article 46 and ICSID Arbitration Rules, Article 40
[224] UNCITRAL Arbitration Rules 1976, Article 19(3).
[225] Trans Pacific Partnership Agreement (2016), Article 9.19(2).

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