Laureate of the Academy' Prize

Is there room for State counterclaims in treaty-based arbitration?

Arbitration law is undoubtedly one of the most dynamic branches of international law. And with accelerated developments come challenges and great questions. The new favourite topic of discussion in conferences and events attended by arbitration lawyers is the backlash the international investment arbitration regime currently faces. Among the criticisms frequently voiced about investment disputes is the so-called asymmetric nature of investment treaties, often allowing foreign investors only to act as claimants. In other words, the system is said to benefit investors only.

Of course, nothing is ever black or white. Within the legal community, it is quite known that States are in fact as successful as investors in investment treaty claims. Nonetheless, a proposition which is increasingly gaining attention is to permit counterclaims to be raised by respondent States in arbitration proceedings.

In this short essay, it will be argued that not only there is room for State counterclaims in treaty-based arbitration, but equally that such proposition may very well constitute an adequate means to address the perceived illegitimacy of the system.

1. The Fundamentals of International Investment Arbitration

One does not need to go very far back in legal history to observe that international investment agreements have been designed to promote and protect foreign investors and their investments

from arbitrary and discriminatory State action. The rationale behind the creation of the impartial dispute settlement mechanism which characterizes investment treaties was indeed to attract foreign investments by guaranteeing legal certainty and procedural fairness to alien investors. In that sense, there is an argument to be made that investors were always meant to be the primary beneficiaries of that system.

This article rather argues that treaty-based arbitration should not only ensure that foreign investors are afforded procedural and substantive protections, but also that investors' conduct is subject to some arbitral oversight. One could go as far as saying that the future of the international investment regime is about shared rights and obligations between States and investors. Therefore, permitting the use of counterclaims by States is in no way contradictory to the fundamentals of treaty-based arbitration.

Furthermore, one shall not forget that such proposition may bear genuine interest for investors. In the event a State wishes to sue a foreign investor for breach of treaty or national law, wouldn't the investor prefer to defend before an arbitral tribunal rather than before a national court which is potentially politically inclined? In line with this, a State which opts for international arbitration to pursue an investment claim signifies the importance it places on the impartial adjudication of investment disputes. For these reasons, this article contends that making greater room for State counterclaims will in principle benefit investors, as well as the investment arbitration system as a whole.

2. Jurisdictional Challenges in Advancing Counterclaims

2.1 Consent

Treaty-based arbitration is an entirely consensual method of dispute resolution and is typically commenced when an investor brings a claim against a State. In fact, by submitting a claim to arbitration, an investor is accepting the State's offer to arbitrate contained in the applicable BIT. This being said, every offer to arbitrate is different. There exist as many offers as there exist investment treaties.

With respect to counterclaims, the main issue is that investment treaties rarely expressly contemplate such possibility, making it rather difficult to ascertain the scope of investors' consent to arbitration. Does the institution of arbitral proceedings encompass consent to defend against potential counterclaims? Arguably so. But again, all deppend on the wording of the applicable investment treaty. Furthermore, it shall be noted that every major arbitration institution has its own rules concerning counterclaims. For instance, Rule 40 of the ICSID Convention provides for arbitral tribunals to determine counterclaims arising directly out of the subject-matter of the initial claim, inasmuch as such possibility is within the scope of the consent of the parties.

In light of the above, there would be room for State counterclaims in treaty-based arbitration to the extent that investment treaties can be read and interpreted as allowing so.

This article wishes to address two questions that are yet to be answered. First, in the absence of precise language in investment treaties, is it sufficient that the offer to arbitrate is neutral as to which party can initiate arbitration proceedings, and does not exclude counterclaims? Accepting

so would imply a liberal reading of investment treaties' dispute resolution clauses. Nevertheless, in the recent *Urbaser v Argentina* ('*Urbaser*') case, it is on that exact basis that the tribunal asserted jurisdiction over the Argentina's counterclaim. Precisely, the tribunal's decision was founded on the open-ended wording of the dispute settlement clause contained in the Spain-Argentina BIT, which simply provided for disputes arising between a State party and an investor to be submitted to international arbitration at the request of either party. Given the neutrality of the provision, the tribunal held that it could not assume that a State could not file for a counterclaim. In 2011, in the *Spyridon Roussalis v Romania* ('*Roussalis*') case, equally decided under the auspices of ICSID, the tribunal recalled that consent by both parties was a *sine qua non* condition to the exercise of its jurisdiction over Romania's counterclaim. However, it ultimately interpreted the notion of *dispute* strictly, as encompassing only issues of compliance by the State with the applicable BIT.

Second, shall the consent of the investor to counterclaims be inferred from its choice to submit a dispute to an institution whose rules expressly confer on the tribunal competence over counterclaims? In the context of ICSID arbitration, a proposition of this kind poses the following problem: Rule 40 of the ICSID Arbitration Rules mentions that the tribunal can assert jurisdiction over a counterclaim, provided that such ancillary claim is within the scope of the consent of the parties. Making the argument that mere consent to ICSID arbitration amounts to consenting to counterclaims would actually render Rule 40 circular, or even void of content. It is the parties' consent to counterclaims which can give effect to Rule 40. Consenting to abide by the ICSID Convention, and therefore Rule 40, cannot replace such consent. Therefore, as held by the tribunal's majority in *Roussalis*, consent must be assessed by reference to the BIT.

Both issues have been discussed in the jurisprudence, but no real judicial trend has arisen yet. There must certaintly be consent to the use of counterclaims in treaty-based arbitration, but whether such consent shall be express, tacit or implied is to be decided on a case-by-case basis. Nonetheless, this article argues that a liberal interpretation of the notion of consent could ensure that the substantive arguments advanced by States in counterclaims are given due consideration. There is indeed a great deal to be said on the merits of counterclaims. Adopting an overly restrictive approach and reducing the debate to purely jurisdictional considerations is antinomical with everything the investment arbitration regime purports to offer: fair and effective dispute settlement proceedings. States do not possess an unfetted right to submit counterclaims, nor investors possess an absolute power to limit tribunals' jurisdiction by simply not consenting to the use of counterclaims for purely tactical reasons. As recalled in *Amco v Indonesia*, investment treaties shall be construed in good faith and in light of the will and expectations of the parties. This article recognizes that parties' expectations towards arbitration are various, and often competing. However, by submitting their disputes to arbitration, both parties shall expect their conduct to be subjected to the scrutiny of the tribunal, to the extent that there is a substantive legal basis on which to perform such assessment, of course.

2.2 Connectedness

For a tribunal to assert jurisdiction over a State counterclaim, a connection between the initial claim and the counterclaim must be established. In this respect, there would be two main approaches. On the one hand, one can argue that it is on the basis of the factual implications of a case that such link exists. In the *Urbaser* case, the tribunal held that a manifest factual connection

was sufficient. Interestingly, the investor's claim was founded on treaty and contractual law, while Argentina's counterclaim was essentially based on international human rights law. Nevertheless, both the initial and the ancillary claims were concerned with the same investment and BIT. On the second hand, one can opt for the approach whereby it is in fact a legal connection that is required. In *Saluka v Czech Republic*, the tribunal interpreted restrictively the connection criterion, requiring the same legal instrument to underly both the claim and the counterclaim.

This article welcomes the conclusion reached in *Urbaser*, as not only investment treaties form part of the applicable law in investment disputes. International and national law may very well apply. Therefore, rejecting a State counterclaim on the basis that it is not entirely founded on the BIT – which is extremely unliekly since BITs do not create direct obligations for investors – would make it nearly unthinkable for States to file counterclaims. An overly strict understanding of the notion of connection would not cope with the multidimensional and international nature of treaty-based arbitration.

3. Grounds for States' Counterclaims

Let alone jurisdictional considerations, the strenght of a counterclaim on the merits is of the utmost importance. As aforementioned, investment treaties typically do not impose obligations upon investors. Hence, the following issue arises: to what rights are States entitled? In other words, on what precise legal basis can States file counterclaims?

Whether rights stemming from national or international law can be given protection in treaty-based arbitration is a matter to be decided on a case-by-case basis. Every BIT has its own

applicable law provision, but most investment treaties specify that 'rules of international law', as well as certain national laws, apply to the relationships and disputes between State parties and investors. For instance, in *Burlington v Ecuador* ('*Burlington*'), the tribunal awarded damages to Ecuador in satisfaction of its counterclaim mainly based on violations of Ecuadorian environmental law by american investors. In *Urbaser*, Argentina's counterclaim was founded on international human rights ('HR') law, and the tribunal recognised that the applicable law to the dispute went beyond the Spain-Argentina BIT and included HR treaties. Although the counterclaim was found to be meritless, one must note the tribunal's statement whereby BITs cannot be construed as isolated sets of rules for the sole purpose of protecting investors. This essay therefore concurs with the argument that States can have grounds to file counterclaims.

4. Justice and Procedural Economy

There is an argument to be made that counterclaims may foster the sound administration of justice and procedural economy. It may very well be contended that the use of counterclaims allows for the adjudication of all connected claims in one single set of arbitral proceedings, and thus in a more efficient, cost-effective and timely manner. In *Urbaser,* the tribunal indeed held that considering separately the investors' claim and Argentina's counterclaim would not reasonably serve the administration of justice and could potentially lead to inconsistent outcomes.

This article concurs with such reasoning. It is not desirable, in many respects, that a dispute which bears complex factual and legal issues be decided by two different tribunals, arbitral and national. In fact, such an eventuality is perhaps absurd, as it seems to counteract the various procedural advantages investment arbitration offers to the parties.

After all, isn't consistency a form of legal certainty, and a feature of a fair dispute settlement exercise?

5. Conclusion

The conceptual, jurisdictional and practical difficulties associated with State counterclaims can only be addressed on a case-by-case basis as every BIT is different. Nevertheless, this essay attempted to demonstrate that there are great arguments to be made in favour of counterclaims. The international investment arbitration community is perhaps witnessing a change in attitude towards the use of counterclaims before tribunals, but in any event, one shall be confident that the values of fairness and efficiency which make the uniqueness of the system will continue to be upheld in investor-State disputes.