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Counterclaims in Investor-State Arbitration

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Article

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ABSTRACT

Although nearly all arbitration rules provide for the right to assert counterclaims in investor-state disputes, many tribunals are reluctant to allow such counterclaims. The two key obstacles examined by tribunals and this Article, are investor consent to counterclaims and determination of investor obligations towards the host State.

Jurisprudence of the Iran-U.S. Claims Tribunal (IUSCT), International Center for Settlement of Investment Disputes (ICSID) tribunals, and United Nations Commission on International Trade Law (UNCITRAL) tribunals suggests that if the relevant treaty contains an offer of jurisdiction only in relation to disputes arising out of State obligations, tribunals are reluctant to extend their jurisdiction over counterclaims. However, if the relevant dispute resolution provision is broad or the parties subsequently alter the jurisdictional offer either explicitly or implicitly, tribunals are more likely to allow counterclaims.

This Article shows that in the absence of provisions setting out investor obligations in international treaties, general principles of law appear to be an appropriate source of international law to determine such obligations. The State may

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also assert counterclaims if the investor breached its obligations under the investment contract concluded with the State. The State, however, cannot assert counterclaims in investor-state arbitration based on purely domestic law obligations of investors.

I. INTRODUCTION

Over the last few decades, States have concluded over 2,500 bilateral investment treaties and numerous multilateral agreements to facilitate foreign investment.[1] According to an almost universal consensus, foreign investments benefit host States by stimulating greater competition, generating an influx of capital, technology, and managerial skills, and creating new jobs.[2] Foreign investors also benefit from access to new markets, a cheaper workforce, and natural resources.[3]

Nearly all investment treaties provide for arbitration to resolve disputes.[4] The system of investor-state dispute resolution endows private persons—either individuals or corporations—with the capacity to submit a claim against a State without the intervention of their respective national governments.[5] Rather than forcing investors to rely either on domestic courts or on State-to-State political negotiations, international investment treaties provide investors with a right to initiate dispute settlements directly against the host State in a neutral forum.[6]

Under these treaties, investors can typically choose to submit a dispute to ICSID or to an *ad hoc* tribunal established

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1. UNCTAD, *Recent Developments in International Investment Agreements (2008-June 2009)*, INT'L INVESTMENT AGREEMENTS MONITOR NO. 3, 2009, *available at* http://www.unctad.org/templates/Page.asp?intItemID=3766&lang=1.

2. *See, e.g.,* Geoffrey Garrett, *The Causes of Globalization*, 33 COMP. POL. STUD. 941, 947 (2000); ORG. FOR ECON. CO-OPERATION AND DEV., FOREIGN DIRECT INVESTMENT FOR DEVELOPMENT: MAXIMISING BENEFITS, MINIMISING COSTS 10–18 (2002); ORG. FOR ECON. CO-OPERATION AND DEV., FDI IN FIGURES (2012), *available at* http://www.oecd.org/dataoecd/60/43/48462282.pdf.

3. *See generally* Garrett, *supra* note 2 (analyzing changes in trade and foreign investment policy that has led to increased international market integration).

4. *See* U.N. CONFERENCE ON TRADE AND DEV., INVESTOR-STATE DISPUTE SETTLEMENT AND IMPACT ON INVESTMENT RULEMAKING, at 78, U.N. Sales No. E.07.II.D.10 (2007).

5. *See* YARASLAU KRYVOI, INTERNATIONAL CENTER FOR SETTLEMENT OF INVESTMENT DISPUTES 26–27 (2010).

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

under the rules of UNCITRAL.[7] Treaties may also provide for dispute resolution procedures of other institutions such as the International Chamber of Commerce (ICC), the Stockholm Chamber of Commerce, or the London Court of International Arbitration.[8]

Because investment treaties are primarily intended to encourage foreign investment, they are usually silent on the rights of States *vis-à-vis* investors and obligations of investors *vis-à-vis* States.[9] Hardwired into the very structure of investment treaties therefore, is an apparent asymmetry between the rights of investors and the obligations of States.

The States' right to counterclaim seeks to counterbalance this asymmetry—counterclaims facilitate equality of the parties and, rendered in a single forum, make investor-state dispute resolution more efficient.[10]

Counterclaims, however, remain relatively rare and tribunals are often reluctant to allow them. It has been suggested that States rarely bring counterclaims because of their counsels' failure to advise them on this matter.[11] Indeed, State counterclaims present a number of particular legal problems: express investor consent to counterclaims or their obligations are absent in treaties, and the nature of the investor-state dispute resolution system is primarily tailored to protect investor interests.[12]

This Article suggests that such constraints should not be fatal to a State's right to assert counterclaims against foreign investors. The right to counterclaim is a procedural right customary to all major arbitration rules, including those used

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7. *See, e.g.,* Treaty Concerning the Reciprocal Encouragement and Protection of Investment. U.S.-Arg., art. VII, Nov. 19, 1991, 31 I.L.M 124 (1992).

8. *See, e.g.*, Agreement Between the Government of the Republic of China and the Government of the Belize on the Protection and Reciprocal Protection of Investments, art. 7, Jan. 16, 1999.

9. *See* RUDOLF DOLZER & CHRISTOPH SCHREUER, PRINCIPLES OF INTERNATIONAL INVESTMENT LAW 7–11 (2008).

10. *See infra* pp. 220–22.

11. Pierre Lalive & Laura Halonen, *On the Availability of Counterclaims in Investment Treaty Arbitration, in* CZECH YEARBOOK OF INTERNATIONAL LAW 141, 154 (Alexander J. Bělohlávek & Naděžda Rozehnalová eds., vol. II 2011).

12. *See* Yaraslau Kryvoi, *Piercing the Corporate Veil in International Arbitration*, 1 GLOBAL BUS. L. REV. 169 (2011) (discussing how undercapitalized local subsidiaries often appear as claimants in arbitral proceedings, and complicate the prospect of obtaining and enforcing arbitral awards against properly capitalized parent companies).

by ICSID or UNCITRAL tribunals.[13] Although investment treaties are typically concluded in the interest of investors, they usually provide for broad jurisdiction over disputes concerning an investment and do not restrict the parties' obligations to only those contained in the investment treaties.[14]

Obligations of investors arise not from the express language of treaties, but out of applicable law, stipulated either in the investment treaty, arbitration agreement or determined by the investor-state tribunal.[15] This Article demonstrates that investor obligations may arise under sources of international law other than investment treaties, such as general principles of law.[16] Secondary sources of international law such as case law and scholarly writings also serve as evidence of international law rules applicable to investors.[17] Under certain circumstances, relevant investor obligations can also be found in investment contracts with States.[18]

The next part of this Article provides an overview of counterclaims, which States asserted under the rules of IUSCT, ICSID, and UNCITRAL. Part III sets forth the main problems related to the requirement of investor consent to counterclaims. Finally, Part IV demonstrates that substantive obligations of investors can be found in sources of international law other than investment treaties, and with certain limitations, in investor-state contracts.

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13. *See, e.g.*, Commission on International Trade Law, G.A. Res. 31/98, art. 19.3 (Dec. 15, 1976) [hereinafter UNCITRAL Arbitration Rules]; Convention on the Settlement of Investment Disputes between States and Nationals of Other States, art. 46, Oct. 16, 1966, 575 U.N.T.S. 159, 17 U.S.T. 1270 [hereinafter ICSID Convention]; THE ARBITRATION INST. OF THE STOCKHOLM CHAMBER OF COMMERCE, RULES OF THE ARBITRATION INSTITUTE OF THE STOCKHOLM CHAMBER OF COMMERCE, art. 10.3, *available at* http://www.sccinstitute.se/filearchive/1/13207/1999_web_a4_vanliga_2004_eng_rev_2005.pdf [hereinafter STOCKHOLM ARBITRATION RULES]; INT'L CTR. FOR SETTLEMENT OF INV. DISPUTES, RULES OF PROCEDURE FOR ARBITRATION PROCEEDINGS, rule 40 [hereinafter ICSID ARBITRATION RULES]; INT'L CHAMBER OF COMMERCE, RULES OF ARBITRATION, art. 5(5) [hereinafter ICC ARBITRATION RULES].

14. *See infra* p. 232.

15. *See infra* p. 232.

16. *See infra* pp. 248–50.

17. *See infra* pp. 250–51.

18. *See infra* pp. 239–42.

II. PROCEDURAL RULES FOR ASSERTING COUNTERCLAIMS

A. INVESTOR-STATE DISPUTES AND COUNTERCLAIMS

A counterclaim in investor-state disputes is a claim submitted by a respondent in opposition to the claimant's claim.[19] Since investors initiate nearly all investor-state disputes,[20] counterclaims are typically submitted by host States. Counterclaims make investor-state arbitration more efficient for a number of reasons.

First, although investment treaties are inherently asymmetrical and provide investors with rights but not obligations, States can initiate and submit counterclaims, which facilitate equality between the parties.[21] Second, counterclaims arising from separate but related agreements between the parties enhance time-efficient dispute resolution.

All major arbitration rules require that counterclaims relate to the substance of the already initiated dispute.[22] Typically, counterclaims have a defensive nature and purport to undermine the primary claim.[23] In the majority of cases in which counterclaims were presented they related to the main

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19. Black's Law Dictionary defines counterclaim as "[a] claim presented by a defendant in opposition to or deduction from the claim of the plaintiff." BLACK'S LAW DICTIONARY 349 (6th ed. 1990) (citing Fed. R. Civ. P. 13). See generally CHRISTIANA FOUNTOULAKIS, SET-OFF DEFENCES IN INTERNATIONAL COMMERCIAL ARBITRATION: A COMPARATIVE ANALYSIS (2010), for a discussion of set-off defences and counterclaims in the context of international arbitration claims.

20. *See The ICSID Caseload – Statistics (Issue 2011-1)*, INT'L CTR. FOR SETTLEMENT INV. DISP., *available at* http://icsid.worldbank.org.

21. *See, e.g.*, Report of the Executive Directors of the International Bank for Reconstruction and Development on the Convention on the Settlement of Investment Disputes between States and Nationals of other States, art. 13, Mar. 18, 1965 (as amended on Apr. 10, 2006), *available at* http://icsid.worldbank.org/ICSID/ICSID/Rulesmain.jsp ("The convention permits the institution of proceedings by host States as well as by investors and the executive directors have constantly had in mind that the provisions of the convention should be equally adapted to the requirements of both cases.").

22. *See, e.g.*, Claims Settlement Declaration Art II, para. 1, 1 Iran-U.S. Cl. Trib. Rep. 9 (1983) (stating that counterclaims from the IUSCT should relate to the matter of the main claims); Commission on International Trade Law, G.A. Res. 31/98, art. 21.3 (Dec. 15, 1976) (as amended in 2010) (stating that counterclaims should be within the tribunal's jurisdiction); ICSID ARBITRATION RULES, *supra* note 13, rule 40 (stating that counter claims must arise "directly out of the subject matter of the dispute").

23. CHRISTOPH SCHREUER ET AL., THE ICSID CONVENTION: A COMMENTARY 750 (2d ed. 2010).

substance of the case and were not of an incidental nature.[24]

Given the high cost of resolving disputes in international arbitration,[25] time-efficient dispute resolution is particularly important for less developed countries. As the dissenting opinion in a recent ICSID case, *Roussalis v. Romania*, pointed out, rejection of jurisdiction over counterclaims may direct the State to its domestic courts and if the judgment would be adverse to the investor, another bilateral investment treaty (BIT) claim may follow.[26] That would result in a duplication of proceedings, inefficiency, and increased transaction costs.[27]

Host States may also be interested in counterclaims because international arbitration offers superior international enforcement prospects compared to domestic court judgments. ICSID arbitration awards do not require any additional procedures for recognition or enforcement: State parties to the ICSID Convention are obligated to enforce the pecuniary obligations imposed by that award within their territories as if it were a final judgment of a court in that State.[28] Most other awards, such as those rendered under UNCITRAL Arbitration Rules, can be enforced under the 1958 New York Convention, which also provides for limited grounds on which awards might be denied enforcement.[29]

There is also a fairness argument. Many suggest that foreign investors often have economic muscle that most host States can hardly surpass.[30] It appears that an unfair asymmetry would arise if the investor could sue the host State for breach of its obligations while the State may not do the same. As the tribunal in *SGS v. Pakistan* put it:

> It would be inequitable if, by reason of the invocation of ICSID jurisdiction, the [foreign investor] could on the one hand

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24. *Id.*

25. *See, e.g.*, Plama Consortium Ltd. v. Republic of Bulgaria, ICSID Case No. ARB/03/24, Award, ¶ 310 (Aug. 27, 2008), http://italaw.com/documents/PlamaBulgariaAward.pdf (stating the legal costs to the claimant (related to both the jurisdiction and merits phases of the arbitration), amounted to $4.6 MM, while the respondent's legal costs (for both phases) were $13.2 MM).

26. Spyridon Roussalis v. Romania, ICSID Case No. ARB/06/1 (2011) (Separate Opinion of Michael Reisman).

27. *Id.*

28. ICSID Convention, *supra* note 13, art. 54.1.

29. Convention on the Recognition and Enforcement of Foreign Arbitral Awards, art. III, June 10, 1958, 21 U.S.T. 2517, 330 U.N.T.S. 3 [hereinafter New York Convention].

30. *See, e.g.,* Karl-Heinz Boeckstiegel, *Enterprise v State: the New David and Goliath*?, 23 ARB. INT'L 93, 95 (2007).

> elevate its side of the dispute to international adjudication and, on the other, preclude the [host State] from pursuing its own claim for damages . . . .[31]

Host States can now assert counterclaims against investors under all major arbitration rules.[32] Most notably, counterclaims have been asserted under IUSCT, ICSID, and UNCITRAL arbitration rules. Despite the view expressed in the literature that counterclaims always fail,[33] the next sections show that this is not always the case.

B. IRAN-US CLAIMS TRIBUNAL

To date, the largest number of counterclaims asserted by States has been under the rules of the IUSCT.[34] The Claims Settlement Declaration, which constitutes the basis of IUSCT jurisdiction, provides that it was

> . . . established for the purpose of deciding claims of nationals of the United States against Iran and claims of nationals of Iran against the United States, and any counterclaim which arises out of the same contract, transaction or occurrence that constitutes the subject matter of that national's claim . . . .[35]

The IUSCT case law suggests that jurisdiction over a counterclaim depends entirely on the presence of jurisdiction over the claim.[36] If jurisdiction over the claim fails, related counterclaims should also be dismissed.[37] If, however, the tribunal asserts its jurisdiction over the counterclaim, it can stand alone, even if the main claim has been withdrawn.[38]

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31. SGS Société Générale de Surveillance S.A. v. Islamic Republic of Pakistan, ICSID Case No. ARB/01/13, Procedural Order No. 2, 395 (Oct. 16, 2002), 8 ICSID Rev.—FILJ 293.

32. *See, e.g.*, UNCITRAL Arbitration Rules, *supra* note 13, art. 19.3; ICSID Convention, *supra* note 13, art. 46; STOCKHOLM ARBITRATION RULES, *supra* note 13, art. 10.3; ICSID ARBITRATION RULES, *supra* note 13, rule 40; ICC ARBITRATION RULES, *supra* note 13, art. 5(5).

33. *See, e.g.*, Ana Vohryzek-Griest, *State Counterclaims in Investor-State Disputes: A History of 30 Years of Failure*, 15 INT'L L., REVISTA COLOMBIANA DE DERECHO INTERNACIONAL 83, 84 (2009) ("State counterclaims in investor-State disputes always fail").

34. *See generally*, CHARLES NELSON BROWER & JASON D. BRUESCHKE, THE IRAN-UNITED STATES CLAIMS TRIBUNAL (1998) (discussing the genesis, structure, and results of the IUSCT).

35. Claims Settlement Declaration, *supra* note 22, at 1.

36. *See, e.g*, Phillips Petroleum Co. Iran v. Iran, 21 Iran-U.S. Cl. Trib. Rep. 79, 146–48 (1989).

37. *Id.*

38. *Id.*

Because IUSCT jurisdiction is defined in rather broad terms, thousands of counterclaims have been filed at the IUSCT.[39] They have included counterclaims for advanced payments, breach of contract, services rendered, defective products, and other categories; all arising out of investor contractual obligations.[40]

C. ICSID CONVENTION

The 1966 ICSID Convention enabled private investors to submit claims against States without intervention of their respective national governments.[41] The Convention and the ICSID Arbitration Rules provide ICSID with jurisdiction over counterclaims.[42] Article 46 of the ICSID Convention stipulates:

> 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.[43]

The ICSID Convention's drafting history suggests that the reason for the inclusion of counterclaims in the Convention was to eliminate the necessity of separate proceedings.[44] The drafters emphasized that counterclaims should be covered by consent of the parties and should not go beyond the tribunal's competence.[45] According to the Report of the Executive Directors of the World Bank, the Convention is meant to be equally adapted to the requirements of the institution of proceedings brought by investors as well as by host States.[46]

Until now, most State counterclaims against foreign investors asserted under ICSID rules were for costs arising out

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39. BROWER & BRUESCHKE, *supra* note 34, at 99.

40. *Id.*

41. YARASLAU KRYVOI, INTERNATIONAL CENTER FOR SETTLEMENT OF INVESTMENT DISPUTES 26–30 (Roger Blanpain et al. eds., 2010).

42. ICSID Convention, *supra* note 13, art. 46; ICSID ARBITRATION RULES, *supra* note 13, art. 40.

43. ICSID Convention, *supra* note 13, art. 46.

44. 2 HISTORY OF THE ICSID CONVENTION: DOCUMENTS CONCERNING THE ORIGIN AND THE FORMATION OF THE CONVENTION ON THE SETTLEMENT OF INVESTMENT DISPUTES BETWEEN STATES AND NATIONALS OF OTHER STATES 270 (2001).

45. *Id.* at 337, 422.

46. Executive Directors of the 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*, ¶ 13, ICSID/15 (Mar. 18, 1965) [hereinafter *ICSID Report*].

of non-ICSID proceedings,[47] interest payments,[48] or taxes.[49] In a majority of ICSID cases, tribunals asserted jurisdiction over counterclaims but subsequently denied them on the merits.[50] In a few other cases, tribunals agreed with the merits of counterclaims asserted by States.[51]

D. UNCITRAL ARBITRAL RULES

The 1976 UNCITRAL Arbitration Rules are commonly used in investor-state disputes.[52] Counterclaims in UNCITRAL investor-state disputes have been rare, which is a consequence of a rather narrow scope of jurisdiction of investment tribunals under the old version of the rules.[53] Until 2010, these rules provided that the respondent could only bring a counterclaim "arising out of the same contract."[54] Currently, the rules, in relevant part, provide as follows:

> In its statement of defense, 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

47. *See, e.g.*, Maritime International Nominees Establishment v. Republic of Guinea, ICSID Case No. ARB/84/4, Award, 76 (Jan. 6, 1988), 4 ISCID Rep. 61 (1997).

48. *See, e.g.*, Benvenuti and Bonfant Srl v. Government of the People's Republic of the Congo, ICSID Case No. ARB/77/2, Award, ¶ 3.5 (Aug. 15, 1980), 1 ISCID Rep. 330 (1993).

49. *See, e.g.*, Amco Asia Corp. et al. v. Republic of Indonesia, ICSID Case No. ARB/81/1, Decision on Jurisdiction, 562–64 (May 10, 1988), 1 ICSID Rep. 543 (1993).

50. *See, e.g.*, Alex Genin v. Republic of Estonia, ICSID Case No. ARB/99/2, Award, ¶¶ 196–201 (June 25, 2001), 17 ICSID Rev. 395 (2002); Southern Pacific Properties (Middle East) Ltd. v. Arab Republic of Egypt, ICSID Case No. ARB/84/3, Decision on Jurisdiction, (Nov. 27, 1985), 3 ICSID Rep. 112 (1995); Klöckner Industrie–Anlagen GmbH v. Republic of Cameroon, ICSID Case No. ARB/81/2, Award, 16 (Oct. 21, 1983), 2 ICSID Rep. 9 (1994); *Benvenuti and Bonfant Srl*, 1 ISCIS Rep. ¶¶ 4.95–4.96; Adriano Gardella SpA v. Government of the Republic of the Ivory Coast, ICSID Case No. ARB/74/1, Award, (Aug. 29, 1977), 1 ICSID Rep. 283 (1993).

51. *See, e.g.*, *Maritime International Nominees Establishment*, 4 ISCID Rep. at 76 (addressing counterclaims for the recovery of legal expenses incurred by the government because of the investor's non-compliance with the tribunal's recommendation).

52. UNCITRAL Arbitration Rules, *supra* note 13.

53. *See*, *e.g.*, Zeevi Holdings v. Republic of Bulgaria, UNCITRAL, Final Award, (Oct. 25, 2006), http://italaw.com/documents/ZeeviHoldingsv.Bulgaria-FinalAward.pdf; Saluka Investments BV v. Czech Republic, UNCITRAL, Decision on Jurisdiction Over the Czech Republic's Counterclaim, ¶¶ 78–79 (May 7, 2004), 15 ICSID Rep. 256 (2010).

54. UNCITRAL Arbitration Rules, *supra* note 13, art. 19.3.

> set-off provided that the arbitral tribunal has jurisdiction over it.[55]

The requirement that a dispute should arise out of the same contract was completely inappropriate in the context of investor-state disputes.[56] More counterclaims are likely to be asserted by States now that the rules have been revised.

As this review of major arbitration rules suggests, investor-state tribunals can assert jurisdiction over counterclaims. There is, however, a legitimate question of whether investors consent to such counterclaims, because most investment treaties do not provide for any obligations of foreign investors and are generally concluded for the benefit of foreign investors who usually initiate arbitral proceedings.

III. CONSENT TO COUNTERCLAIMS

A. INVESTOR CONSENT TO COUNTERCLAIMS

Historically, the main aim of investment treaties and contracts was to moderate the exercise of sovereign power by host States.[57] Only States have a monopoly on using force to regulate activities of all economic actors in their own territory. The idea behind investment treaties is that it is the conduct of States, rather than the conduct of investors, which needs to be kept in check.[58]

Today most treaties explicitly provide that their main goal is to protect investors and facilitate foreign investments.[59] Investors are privileged and "traditionally [have been] afforded rights without being subject to obligations. . . ."[60]

Investors' legal position under investment treaties can be compared to that of third party beneficiaries in contracts—they

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55. Commission on International Trade Law, *supra* note 22, art. 21.3.

56. *See* JAN PAULSSON & GEORGIOS PETROCHILOS, REVISION OF THE UNCITRAL ARBITRATION RULES (2006), *available at* http://www.uncitral.org/pdf/english/news/arbrules_report.pdf.

57. *See* Kenneth J. Vandevelde, *A Brief History of International Investment Agreements*, 12 U.C. DAVIS J. INT'L L. & POL'Y 157, 193 (2005).

58. *See* Gustavo Laborde, *The Case for Host State Claims in Investment Arbitration*, 1 J. INT'L DISP. SETTLEMENT 97, 98 (2010).

59. *See*, *e.g.*, Agreement for the Promotion and Protection of Investments, U.K.–Kaz., Preamble, Nov. 23, 1995, GR. BRIT. T.S. NO. 30 (1996) (Cm. 3176) ("Desiring to create favourable conditions for greater investment by nationals and companies of one State in the territory of the other State.").

60. MARC JACOB, INTERNATIONAL INVESTMENT AGREEMENTS AND HUMAN RIGHTS 21 (2010).

have rights but not obligations.[61] Treaties typically only enable the investor, rather than the State, to submit claims to arbitration.[62] Investment treaties typically neither provide for the submission of a State's counterclaims nor even mention the right of an investor to submit counter-claims.[63] Some scholars even dub investment arbitration as an international " 'quasi-judicial review' of national regulatory action."[64]

Like all international treaties, investment treaties are supposed to be interpreted in light of their object and purpose.[65] In the absence of any specific language providing for a possibility of counterclaims against foreign investors, allowing such counterclaims may seem problematic. Consent remains a cornerstone of the system of international adjudication in general[66] and investor-state arbitration in particular.[67]

If the investor limited its acceptance of jurisdiction to claims based on the treaty, should only the treaty be the source of rights and obligations in a particular dispute? To answer this question, it is important to understand that the investment treaty itself is not the basis for the tribunal's jurisdiction. Investors are not parties to international treaties, and therefore, cannot consent to arbitration *in* such treaties.

When a State enters into an investment treaty, it offers eligible investors a right to arbitrate any relevant investment disputes through international arbitration.[68] If the investor chooses to accept the offer, it usually does so by initiating arbitration proceedings, thereby perfecting the parties'

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61. Laborde, *supra* note 58, at 112.

62. *See, e.g.*, Agreement for the Promotion and Reciprocal Protection of Investments, Greece–Rom., May 23, 1997, art. 9.2.

63. *See id.*

64. Hege Elisabeth Veenstra–Kjos, *Counter-claims by Host States in Investment Dispute Arbitration "Without Privity"*, *in* NEW ASPECTS OF INTERNATIONAL INVESTMENT LAW 597, 600 (Philippe Kahn & Thomas W. Wälde eds., 2007); *see also* Gus van Harten & Martin Loughlin, *Investment Treaty Arbitration as a Species of Global Administrative Law*, 17 EUR. J. INT'L L. 121 (2006).

65. Vienna Convention on the Law of Treaties art. 31.1, May 23, 1969, 1155 U.N.T.S. 331 ("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.").

66. ELIHU LAUTERPACHT, ASPECTS OF ADMINISTRATION OF INTERNATIONAL JUSTICE 23 (1991).

67. *See ICSID Report*, *supra* note 46, ¶ 23.

68. *See* LUCY REED, JAN PAULSSON & NIGEL BLACKABY, GUIDE TO ICSID ARBITRATION 35 (2004); Jan Paulsson, *Arbitration Without Privity*, 10 ICSID REV. – FOREIGN INVESTMENT L.J. 232 (1995).

agreement to arbitrate the investment dispute.[69] An investor's consent to arbitration can also be manifested in a separate agreement with the State to arbitrate a claim under the investment treaty.[70]

Such consent typically incorporates by reference a certain set of arbitration rules, which the parties agree to apply in full. Neither such agreements nor requests for arbitration usually contain an express reference to counterclaims.[71] But narrow wording of acceptance of the offer to arbitrate disputes should not have the effect of excluding State counterclaims because [a] BIT is not an *á la carte* selection of provisions among which the investor can chose.[72] If the arbitration rules include the procedural right to submit counterclaims,[73] the parties are bound by it.[74]

Moreover, in a number of disputes, States themselves initiated ICSID proceedings against investors under investment treaties,[75] which makes the submission of counterclaims a less controversial issue. But as the analysis below suggests the narrow wording of a relevant dispute resolution treaty provision may affect the tribunal's subject matter jurisdiction.

In *AMTO v. Ukraine,* a dispute arose on the basis of the Energy Charter Treaty (ECT) and the Rules of the Arbitration Institute of the Stockholm Chamber of Commerce (SCC).[76] ECT contains no mentioning of the right to counterclaim and covers only disputes arising out of obligations of States:

> Disputes between a Contracting Party and an Investor of another Contracting Party relating to an Investment of the latter in the Area of the former, which concern an alleged breach of an obligation of the former under [the ECT].[77]

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69. *See* REED ET AL., *supra* note 68, at 35; Paulsson, *supra* note 68.

70. *See* REED ET AL., *supra* note 68, at 36; Paulsson, *supra* note 68.

71. Lalive & Halonen, *supra* note 11, at 149.

72. *Id.* at 150.

73. As explained above, the ICSID Convention, UNCITRAL Arbitration Rules, and other arbitration rules explicitly provide for the right to assert counterclaims. *See supra* note 13 and accompanying text.

74. *See* Pierre A. Karrer, *Jurisdiction on Set–off Defences and Counterclaims*, 67 Arb. 176, 177 (2001) ("[A]n arbitral tribunal should have jurisdiction over counterclaims between the same parties, even if these counterclaims are not covered by the arbitration agreement which confers jurisdiction on the arbitral tribunal over the main claim [. . .].").

75. Laborde, *supra* note 58, at 100.

76. Limited Liability Company AMTO v. Ukraine, SCC Case No. 080/2005, Final Award, (Mar. 26, 2008), http://italaw.com/documents/AmtoAward.pdf.

77. Energy Charter Treaty art. 26.1, Dec. 17, 1994, 34 I.L.M. 360

The State relied on Article 10 of the SCC rules and asserted a counterclaim for non-material injury to its reputation.[78] The tribunal ruled that counterclaims were outside of its jurisdiction because the State failed to specify the basis for its counterclaim in applicable law:

> . . . the jurisdiction of an Arbitral Tribunal over a State Party counterclaim under an investment treaty depends upon the terms of the dispute resolution provision of the treaty, the nature of the counterclaim and the relationship of the counterclaims with the claims in arbitration.[79]

The tribunal in that case decided it could not go beyond its subject matter jurisdiction and declined to assert jurisdiction over the counterclaim.[80] Had the ECT covered a wider category of disputes or provided for investor obligations, the outcome could have been different.[81]

The ICSID tribunal in *Roussalis v. Romania* recently rejected respondent's counterclaim on the basis of an absence of the investor's consent.[82] The tribunal focused on the dispute resolution clause of the BIT, which provided for resolution of disputes concerning obligations of the State.[83]

The majority in that case reasoned that the relevant BIT language which refers to "disputes . . . concerning an obligation of the latter" limited jurisdiction to claims brought by investors about obligations of the host State.[84] The arbitrators further

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[hereinafter ECT].

78. *AMTO,* SCC Case No. 080/2005 §§ 116–18. The SCC Arbitration Rules provided for the right to counterclaim. *See* STOCKHOLM ARBITRATION RULES, s*upra* note 13, art. 10.

79. *AMTO,* SCC Case No. 080/2005 § 118.

80. *Id.*

81. The North American Free Trade Agreement (NAFTA) may also present the same problem. The NAFTA dispute settlement clause is limited to obligations under specified articles of NAFTA. Under Articles 1116 and 1117 of NAFTA, the only claims which may be submitted to arbitration are claims alleging that another NAFTA Party has breached an obligation under specified articles of Chapter 11. North American Free Trade Agreement, U.S.-Can.-Mex., Dec. 17, 1992, 32 I.L.M 289 (1993) [hereinafter NAFTA].

82. Spyridon Roussalis v. Romania, ICSID Case No. ARB/06/1, Award, ¶¶ 864–76 (Dec. 7, 2011), http://icsid.worldbank.org/ICSID/FrontServlet?requestType=CasesRH&actionVal=showDoc&docId=DC2431_En&caseId=C70.

83. The Romania-Greece BIT provided for jurisdiction in "[d]isputes between an investor of a Contracting Party and the other Contracting Party concerning an obligation of the latter under this Agreement, in relation to an investment of the former." Agreement for the Promotion and Reciprocal Protection of Investments, *supra* note 62, art. 9.1.

84. *Spyridon Roussalis*, ICSID Case No. ARB/06/1 ¶ 869.

explained that "where the BIT does specify that the applicable law is the BIT itself, counterclaims fall outside the tribunal's jurisdiction."[85] Because the BIT did not impose any obligations on the investor, counterclaims, according to the majority, fall outside of the tribunal's jurisdiction.[86]

Professor Michael Reisman wrote a sharp dissent in *Roussalis v. Romania* in which he criticized the majority's refusal to consider counterclaims on the merits as "an ironic, if not absurd, outcome, at odds . . . with the objectives of international investment law."[87] In his view, consent to ICSID jurisdiction *ipso facto* includes consent to Article 46 of the ICSID Convention, which provides for the right to counterclaim both to the State and to the investor.[88]

The Resiman's position is not unprecedented. The ICSID tribunal in *Hamester v. Ghana* considered a BIT clause similar to the one in *Romania v. Roussalis* which provided that the parties consent to disputes "concerning an obligation of [the host State] under this Treaty in relation to an investment of [a national or company of the other Contracting Party]."[89] Strict treaty interpretation would suggest that counterclaims would not fall under the tribunal's jurisdiction because the investor was not a party to the treaty and the treaty did not provide for obligations of investors. The tribunal, however, observed that under this treaty a State could also be an aggrieved party and refer disputes to arbitration.[90]

In another case, *Saluka v. Czech Republic*, the relevant dispute resolution clause covered a much wider spectrum of

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85. *Id.* ¶ 871.

86. *Id.* The Majority's view that the BIT is the applicable law seems controversial because the parties explicitly chose Romanian law to govern the merits of the dispute. *Id.* ¶ 306. Additionally, provisions of the BIT establish that "the applicable rules and principles of international law" should apply to the dispute. Agreement for the Promotion and Reciprocal Protection of Investments, *supra* note 62, art. 9.4.

87. *Spyridon Roussalis*, ICSID Case No. ARB/06/1 (Separate Opinion of Michael Reisman).

88. *See id.*

89. Gustav F W Hamester GmbH & Co KG v. Republic of Ghana, ICSID Case No. ARB/07/24, Award, ¶ 354 (June 18, 2010), http://italaw.com/documents/Hamesterv.GhanaAward.pdf (quoting Treaty for the Encouragement and Reciprocal Protection of Investments, Ger.–Ghana, Feb. 24, 1995, *available at* http://www.unctad.org/sections/dite/iia/docs/bits/germany_ghana.gr.pdf).

90. *Gustav F W Hamester*, ICSID Case No. ARB/07/24 ¶¶ 351–52. Eventually the tribunal ruled not to consider counterclaims any further, because the State failed to properly submit on the nature of counterclaims under the BIT. *Id.* ¶ 355.

disputes, specifically: "[a]ll disputes between one Contracting Party and an investor of the other Contracting Party concerning an investment of the latter."[91] The tribunal explained:

> 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.[92]

This analysis of case law suggests that if the relevant dispute resolution treaty provision is broad enough and is not limited to obligations specifically provided by the treaty, the tribunals are more likely to assert counterclaims against investors. But as explained below, even in the context of broadly formulated dispute resolution clauses, not all investor obligations fall under the subject matter jurisdiction of investor-state tribunals.[93]

B. CONSENT TO COUNTERCLAIMS AGAINST AFFILIATED COMPANIES

Does foreign investor consent cover counterclaims against affiliated parties, such as a parent company? Often the formal claimant in arbitral proceedings is a local subsidiary incorporated as a distinct corporate entity.[94] Its parent company is protected from the subsidiary's obligations by the principle of limited liability.[95] These local subsidiaries could be undercapitalized and unable to pay any award rendered

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91. Agreement on Encouragement and Reciprocal Protection of Investments Between the Kingdom of the Netherlands and the Czech and Slovak Federal Republic, art. 8, Apr. 9, 1991, 2242 U.N.T.S. 205 [hereinafter Netherlands Agreement].

92. Saluka Investments BV v. Czech Republic, UNCITRAL, Decision on Jurisdiction Over the Czech Republic's Counterclaim, ¶ 39 (May 7, 2004), 15 ICSID Rep. 256 (2010). The *Saluka* tribunal subsequently decided that it had no jurisdiction over the counterclaim, primarily because of the lack of a close connection between the original claim and the counterclaim, which the tribunal deemed to be a matter of Czech law and not something that fell under the Agreement. *See id.* ¶¶ 79–82.

93. *See infra* Part IV.A–C.

94. *See, e.g.*, Pierre Lalive, *The First 'World Bank' Arbitration (Holiday Inns v. Morocco)—Some Legal Problems*, 51(1) BRIT. Y.B. INT'L L. 123, 128 (1980) (explaining that the claimant in *Holiday Inns v. Morocco* was a subsidiary that had not been fully formed at the time the agreement was made, but that the tribunal still recognized its jurisdiction over the claim); *see also* Kryvoi, *supra* note 12, at 184–86.

95. *See, e.g.,* Kryvoi, *supra* note 12, at 171–73 (explaining that limited liability is one of the main rationales behind the corporate form and that creating subsidiary companies can further shield business owners from risk).

against them.[96] It may be difficult, if at all possible, to make a parent company with deeper pockets a party to arbitral proceedings.[97]

When a State-affiliated entity signs a contract, investors can extend the clause to the State as a whole. The International Law Commission Articles on State Responsibility explain when an entity is considered to be acting with the authority of the State.

An entity whose structure, function, and control flows from governmental authority, as well as the conduct of persons empowered by the State to "exercise elements of the governmental authority," is considered to be acting with the authority of the State "provided the person or entity is acting in that capacity in the particular instance."[98] It is more difficult for States to counterclaim against corporations that have not signed the arbitration agreement. This is yet another manifestation of the pro-investor asymmetry of investor-state arbitration.

An ICSID tribunal analyzed whether to pierce the corporate veil when faced with asserted counterclaims in *Klöckner v. Cameroon*.[99] The tribunal asserted its jurisdiction and permitted the State to assert a counterclaim that involved a locally incorporated subsidiary, SOCAME.[100] The Cameroonian government signed several agreements with the claimant, Klöckner, and its domestically incorporated company,

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96. *See, e.g., id.* at 173 ("A typical corporate veil piercing case involves a controlling shareholder who sets up an undercapitalized corporation to incur obligations to a third party.").

97. *See id.* for a more detailed discussion of piercing the corporate veil.

98. Responsibility of States for Internationally Wrongful Acts, G.A. Res. 83, U.N. GAOR, 56th Sess., Supp. No. 10, U.N. Doc. A/Res/56/83, art. 5 (Jan. 28, 2002). But not all affiliated entities' actions are regarded as actions of the State; instead, only those actions where the State acts as a sovereign. *See*, *e.g.*, Bayindir Insaat Turizm Ticaret VE Sanay A.S. v. Islamic Republic of Pakistan, ICSID Case No. ARB/03/29, Award, ¶ 444 (Aug. 27, 2009), http://italaw.com/documents/Bayandiraward.pdf ("[T]his inquiry consists in examining whether the alleged interference with the property or the rights of the investor has been made in the State's exercise of its sovereign powers."); Siemens AG v. Argentine Republic, ICSID Case No. ARB/02/8, Award, ¶ 253 (Feb. 6, 2007), 14 ICSID Rep. 518 (2009) ("[F]or the State to incur international responsibility it must act as such, it must use its public authority."); IAN BROWNLIE, PRINCIPLES OF PUBLIC INTERNATIONAL LAW 547 (2008).

99. Klöckner Industrie-Anlagen GmbH v. Republic of Cameroon, ICSID Case No. ARB/81/2, Award, 13–18 (Oct. 21, 1983), 2 ICSID Rep. 9 (1994).

100. *See id.* at 15–16 (noting that the subsidiary SOCAME was under foreign control at the time the agreements were signed between the parties, which brought it under the arbitration agreement).

SOCAME, which stipulated that ICSID arbitration would be used in the event of disputes.[101] When the issue of counterclaims against a locally incorporated company arose, the arbitrators focused on subject matter jurisdiction over the contract to ultimately allow the counterclaims to move forward, instead of focusing on ICSID's personal jurisdiction over a non-signatory to the arbitration agreement.[102]

The *Klöckner* tribunal explained that the main question was not whether the tribunal had jurisdiction "*ratione personae*" over the locally incorporated company,[103] but rather whether it had jurisdiction "*ratione materiae*" on the application and interpretation of the Establishment Agreement.[104] The tribunal concluded that the contracts entered into by a local subsidiary establish the jurisdiction of the tribunal with respect to the counterclaim because there was a direct connection between the contracts and the parties' claims.[105]

In *Saluka v. Czech Republic*, a UNCITRAL case, the investor contended that the tribunal had no personal jurisdiction over the entity against which the State asserted a counterclaim because that entity had never consented to be a party to the arbitration.[106] The State responded that if the locally incorporated entity was permitted to represent the interests of the foreign parent company in arbitration, a counterclaim could be asserted against the foreign parent company.[107] The State asked to pierce the corporate veil and treat both companies as "the same single group of companies"

101. *See id.* at 13–18 (detailing the different agreements signed between the companies and Cameroon, and the resulting disputes).

102. *Id.* at 17 ("The question before the present Tribunal is . . . to determine whether it has jurisdiction '*ratione materiae*' to rule on the application and interpretation of the Establishment Agreement.").

103. *See id.* (explaining that the foreign company was acting through the local company, meaning that the contract was actually between the foreign company and the host country, Cameroon).

104. *See id.* (noting that the Establishment Agreement should be taken together with the Protocol of Agreement and the Supply Contract, which when combined give the Arbitral Tribunal jurisdiction).

105. Klöckner Industrie-Anlagen GmbH v. Republic of Cameroon, ICSID Case No. ARB/81/2, Award, 8 (Oct. 21, 1983), 2 ICSID Rep. 9 (1994) ("The three contracts establish the jurisdiction of the tribunal with respect to the counterclaim, given the direct connection between the three instruments and the parties' claims.").

106. Saluka Investments BV v. Czech Republic, UNCITRAL, Decision on Jurisdiction over the Czech Republic's Counterclaim, ¶ 25 (May 7, 2004), 15 ICSID Rep. 256 (2010).

107. *Id.* ¶ 29.

to redress abuse of the corporate form.[108] The *Saluka* tribunal refrained from ruling on the issue of piercing the corporate veil and merely assumed that

> the relationship between [the affiliated companies] is sufficiently close to enable the Tribunal's jurisdiction in proceedings instituted by [the local subsidiary] to extend to claims against [the parent company].[109]

The tribunal ultimately held that it did not have jurisdiction for two reasons: first, because there was an absence of a close connection between the primary claim and the counterclaim;[110] and second, because the contract established a special dispute resolution procedure for the issues contested in the counterclaim.[111]

It appears that tribunals are reluctant to pierce the corporate veil in the counterclaim context because counterclaims may fall outside of the parties' consent to arbitration. Even if a tribunal decides to assert jurisdiction over affiliated companies, the party enforcing the resulting award may face serious challenges.[112] Enforcing awards against parent companies located in other countries in the absence of their explicit consent to arbitration requires piercing the corporate veil, which can be problematic under applicable arbitration rules, relevant domestic law, and the New York Convention.[113] The only exception is an award granted under the ICSID Convention. Such award should be enforced as if it is a final judgment of a domestic court of that State.[114]

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108. *Id.*

109. *Id.* ¶ 44.

110. *Id.* ¶¶ 47–82 ("[T]he disputes which have given rise to the Respondent's counterclaim are not sufficiently closely connected with the subject matter of the original claim put forward by Saluka to fall within the Tribunal's jurisdiction."). *But see* Lalive & Halonen, *supra* note 11, at 157 ("[C]ommentators have also criticised the connection required in *Klöckner* and *Saluka* as being too demanding, suggesting that a close factual nexus should be enough or that the fact that the counterclaim arises from the same 'investment' as the claim suffices."); ZACHARY DOUGLAS, THE INTERNATIONAL LAW OF INVESTMENT CLAIMS 260–63 (2009) (explaining the different outcomes in different tribunals in regards to the requirement of a "requisite nexus").

111. Saluka Investments BV v. Czech Republic, UNCITRAL, Decision on Jurisdiction over the Czech Republic's Counterclaim, ¶¶ 47–82 (May 7, 2004), 15 ICSID Rep. 256 (2010).

112. *See, e.g.*, Kryvoi, *supra* note 12, 175–77 (explaining the different legal grounds on which an affiliated company party may assert in order to challenge an arbitration award).

113. *Id.*

114. ICSID Convention, *supra* note 13, art. 54.1 ("A Contracting State with a federal constitution may enforce such an award in or through its federal

The next section analyzes in more detail whether foreign investors have not only rights but also international obligations *vis-à-vis* host States.

IV. SUBSTANTIVE OBLIGATIONS OF INVESTORS IN INVESTOR-STATE DISPUTES

A. INVESTORS AS BEARERS OF INTERNATIONAL OBLIGATIONS

According to the traditional doctrine of international law, only States, not individuals, can be the subjects of obligation and responsibility in international law.[115] Until the second half of the Twentieth century, the dominant principle of international law was that a wrong done to a national of one State, for which another State was intentionally responsible, was not actionable by the injured national, but instead was only actionable by his State.[116] Investors were not able to proceed with an international claim against a foreign government directly.[117]

In the past, foreign investors had to seek the diplomatic protection of their home State to support their case and to initiate proceedings before an international tribunal.[118] In recent years, the legal status of investors in international law has been shifting from this classical position to the recognition of an increased role of individual rights.[119]

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courts and may provide that such courts shall treat the award as if it were a final judgment of the courts of a constituent state.").

115. *See, e.g.*, HANS KELSEN, PRINCIPLES OF INTERNATIONAL LAW 194 (1966) ("The traditional doctrine that only states, not individuals, are the subjects of international law means that the personal sphere of validity of the international legal order is limited.").

116. *See generally* Eduardo Jimenez de Arechaga, *Diplomatic Protection of Shareholders in International Law*, 4 PHIL. INT'L L.J. (1965) (explaining diplomatic and judicial protection in greater detail).

117. KELSEN, *supra* note 115, at 194 (discussing how the traditional doctrine of international law only conferred rights upon States, meaning that individuals did not have rights and therefore could not bring suit against States).

118. *See* KRYVOI, *supra* note 5, at 26 (explaining that investor inability to reach States through legal suits was one of the reasons for the formation of ICSID).

119. *See generally* PETER T. MUCHLINSKI, MULTINATIONAL ENTERPRISES AND THE LAW (2007) (discussing the evolving status of multinational enterprises); DAVID IJALAYE, THE EXTENSION OF INTERNATIONAL PERSONALITY IN INTERNATIONAL LAW 221–37 (1978) (explaining that private companies doing foreign business have developed a legal footing similar to that of States, even though this position in international law is challenged by some).

One of earliest examples recognizing an individual's civil responsibility is the International Convention for the Protection of Submarine Telegraph Cables, which provided that an individual who broke a submarine cable had an obligation to pay for the cost of repair of the cable.[120] Individual responsibility is also recognized under international law, for example, in cases of piracy, breach of blockade, carriage of contraband, and acts of illegitimate warfare.[121]

In theory, subjects of international law are "persons to whom international law attributes rights and duties directly and not through the medium of their states."[122] In the investor-state context, tribunals assume that investors have the capacity to contract for the right to sue States in investor-state disputes.[123] As the sole arbitrator in *Texaco v. Libya* explained: "[F]or the purposes of interpretation and performance of the contract, it should be recognized that a private contracting party has specific international capacities."[124]

Individual investors can now initiate an action against a State before a tribunal, the jurisdiction of which the State is obliged to recognize.[125] Investor rights to sue States in investor-state disputes was a significant advancement of the status of individuals compared to claims commissions, which States had previously used to resolve investor grievances.[126] As discussed above, international law also imposes certain obligations on foreign investors directly that are not attributable through the medium of States.[127]

The primary source of investor obligations in international

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120. International Convention for the Protection of Submarine Telegraph Cables art. IV, Mar. 4, 1884, T.S. No. 380, *available at* http://cil.nus.edu.sg/1902/1884-convention-for-the-protection-of-submarine-telegraph-cables/.

121. *See* IJALAYE, *supra* note 119, at 203–07.

122. Marek St. Korowicz, *The Problem of the International Personality of Individuals*, 50 AM. J. INT'L L. 533, 535 (1956).

123. *See* ELIHU LAUTERPACHT, ASPECTS OF ADMINISTRATION OF INTERNATIONAL JUSTICE 67–72 (1991).

124. Texaco Overseas Petroleum Co./Cal. Asiatic Oil Co. v. Government of the Libyan Arab Republic, Award, ¶ 47 (Jan. 19, 1977), 17 I.L.M. 1 (1978).

125. *See, e.g.*, KELSEN, *supra* note 115, at 221–22 ("International law, especially a treaty, confers rights on individuals by authorizing private persons to bring a lawsuit against a state before a national or an international tribunal.").

126. *See, e.g.*, Treaty of Peace with Italy art. 83, Feb. 10, 1947, 61 Stat. 1245 (establishing conciliation commissions); Treaty of Peace with Japan art. 4, Sept. 8, 1951, 59 Stat. 1031 (establishing property commissions).

127. *See supra* notes 115–125 and accompanying text.

arbitration is the applicable law agreed upon by the parties.[128] Relevant international investment treaties may contain choice of law provisions. For instance, the treaty in *Saluka v. Czech Republic* provided for the use of the domestic law of the host State, provisions of the BIT and other agreements between the parties, "provisions of special agreements related to the investment," and the "general principles of law."[129] As explained below, investment treaties are often silent on the issue of applicable law and even when domestic law is chosen, not all domestic law obligations rise to a level arbitable at the international level.

B. DOMESTIC LAW AS A SOURCE OF INTERNATIONAL OBLIGATIONS

Investment treaties usually contain no provisions on the issue of applicable law.[130] In some cases, investment treaties refer both to domestic law and international law as applicable law.[131] In other cases, treaties are unclear about which law is applicable.[132] According to the ICSID Convention, if the parties fail to agree on applicable law, the law of the host State applies.[133] UNCITRAL Arbitration Rules as well as other institutional arbitration rules give discretion to the tribunal to determine what law should apply in such situations.[134]

Investor failure to comply with the laws of the host State may act to exclude the investment from protection under the investment treaty. For example, in *Maffezini v. Spain*, the tribunal held that the Argentine investor's failure to comply with its environmental regulations constituted a violation of

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128. ICSID Convention, *supra* note 13, art. 42.1 ("The Tribunal shall decide a dispute in accordance with such rules of law as may be agreed by the parties. In the absence of such agreement, the Tribunal shall apply the law of the Contracting State party . . . and such rules of international law as may be applicable.").

129. Netherlands Agreement, *supra* note 91, art. 8.6.

130. *See* Antonio R. Parra, *Applicable Law in Investor-State Arbitration*, *in* CONTEMPORARY ISSUES IN INTERNATIONAL ARBITRATION AND MEDIATION: THE FORDHAM PAPERS 2007 3, 7–8 (Arthur W. Rovine ed., 2007).

131. *See, e.g.*, TAIDA BEGIC, APPLICABLE LAW IN INTERNATIONAL INVESTMENT DISPUTES 232 (2005).

132. *Id.* (explaining that often treaties are written in a way that makes the parties' choice of law "not . . . clear and explicit").

133. ICSID Convention, *supra* note 13, art. 42.1.

134. UNCITRAL Arbitration Rules, *supra* note 13, rule 35.1 (stipulating that the tribunal must apply the law that is chosen by the parties, but also noting that if the parties fail to identify which law should apply, the tribunal will elect the applicable law for them).

the investor's obligations.[135] In the 2006 case, *Inceysa v. El Salvador,* the tribunal declined jurisdiction on the basis of an investment treaty provision that the investment must be made in accordance with the laws of the host country.[136] The tribunal held that an investment made through fraudulent means could not be made in accordance with law.[137]

Although applicable domestic law contemplates investor obligations, not all domestic law obligations rise to the level of international law obligations. Counterclaims arising out of the application of domestic law of general applicability usually fall outside of the international tribunals' jurisdictions.

For instance, in a number of cases before the IUSCT, Iran counterclaimed requesting allegedly unpaid taxes and social security contributions.[138] The IUSCT tribunals usually held that such counterclaims arise not out of the contracts that were the subject matter of the investor's claim, but out of the generally applicable domestic law.[139] This approach remained the same even if the contract upon which a claim was based expressly allocated the burden to comply with such domestic law requirements to the claimant.[140]

A good example of an ICSID case with the same logic is *Amco v. Indonesia*, in which the State asserted a counterclaim seeking payment of taxes and customs duties.[141] Subsequently, Indonesia modified its counterclaim and alleged tax fraud.[142] The tribunal eventually ruled that because the claim did not arise "directly out of an investment," as required by the ICSID

135. *See* Maffezini v. Kingdom of Spain, ICSID Case No. ARB/97/7, Award, (Nov. 13, 2000), 5 ICSID Rep. 419 (2002).

136. Inceysa Vallisoletana, S.L. v. Republic of El Salvador, ICSID Case No. ARB/03/26, Award (Aug. 2, 2006), http://italaw.com/documents/Inceysa_Vallisoletana_en_001.pdf.

137. *Id.* ¶¶ 230–64 (analyzing the fraudulent actions under international and El Salvadoran law).

138. Petrolane, Inc. v. Iran, 27 Iran-U.S. Cl. Trib. Rep. 64, ¶ 118 (1991); Questech, Inc. v. Ministry of Nat'l Def. of Islamic Republic of Iran, 9 Iran-U.S. Cl. Trib. Rep. 107, 134–36 (1985).

139. *Petrolane, Inc.*, 27 Iran-U.S. Cl. Trib. Rep. 64, ¶ 118; *Questech, Inc.*, 9 Iran-U.S. Cl. Trib. Rep. at 134–36.

140. *See, e.g.*, Int'l Technical Prods. Corp. v. Iran, 9 Iran-U.S. Cl. Trib. Rep. 206, 224–26 (1985).

141. Amco Asia Corp. et al. v. Republic of Indonesia, ICSID Case No. ARB/81/1, Award, ¶¶ 283–87 (Nov. 20, 1984), 1 ICSID Rep. 413 (1993).

142. Amco Asia Corp. et al. v. Republic of Indonesia, ICSID Case No. ARB/81/1, Resubmitted Case: Decision on Jurisdiction, 562–64 (May 10, 1988), 1 ICSID Rep. 543 (1993). The tribunal considered the tax fraud as a new claim because Indonesia did not introduce it as a counterclaim in accordance with ICSID Arbitration Rules. *Id.* at 564–65.

Convention, the tax fraud case was outside its jurisdiction.[143] The tribunal also distinguished between rights and obligations provided by the investment treaty and generally applicable rights and obligations:

> [I]t is correct to distinguish between rights and obligations that are applicable to legal or natural persons who are within the reach of a host State's jurisdiction, as a matter of general law; and rights and obligations that are applicable to an investor as a consequence of an investment agreement entered into with that host State.
>
> Legal disputes relating to the latter will fall under Article 25(1) of the Convention. Legal disputes concerning the former, in principle, are to be decided by the appropriate procedures in the relevant jurisdiction unless the general law generates an investment dispute under the Convention.[144]

The same logic on arbitrability of domestic law claims in investor-state arbitration appeared in *Saluka v. Czech Republic*, a dispute governed by UNCITRAL rules.[145] Like in *Amco v. Indonesia*, the tribunal emphasized that the counterclaims involved "non-compliance with the general law of the Czech Republic" and "rights and obligations which are applicable, as a matter of the general law of the Czech Republic, to persons subject to the Czech Republic's jurisdiction."[146] The tribunal concluded that the counterclaims were to be decided not through the investment treaty settlement procedure, but through appropriate procedures under Czech law.[147]

More recently, a UNCITRAL tribunal was asked to decide a tax counterclaim in *Paushok v. Mongolia*.[148] The tribunal ruled the claim was outside its jurisdiction because the claim arose out of the public law of Mongolia.[149] It explained its decision:

> [T]hrough the Counterclaims the Respondent seeks to

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143. *Id.* at 565.

144. *Id.*

145. Saluka Investments BV v. Czech Republic, UNCITRAL, Decision on Jurisdiction over Czech Republic's Counterclaim, ¶¶ 78–79 (May 7, 2004), 15 ICSID Rep. 256 (2010) (applying UNCITRAL Arbitration Rules).

146. *Id.*

147. *Id.* ¶ 79.

148. *See* Sergei Paushok v. Government of Mongolia, UNCITRAL, Award on Jurisdiction and Liability, ¶ 678 (Apr. 28, 2011), http://italaw.com/documents/PaushokAward.pdf.

149. *Id.* ¶¶ 684–99.

> 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, since the generally accepted principle is the non-extraterritorial enforceability of national public laws and, specifically, of national tax laws.[150]

General measures such as tax or economic policy are normally outside the jurisdiction of investor-state tribunals as long as they do not result in a violation of prior international law commitments.[151] But if such measures have a specific effect on the violation of preexisting commitments, they may fall under the jurisdiction of arbitral tribunals.[152]

In summary, counterclaims can be based on domestic law obligations of investors only if those same obligations were specifically mentioned in the relevant investment treaty or otherwise committed to by the parties. Violation of purely domestic law obligations is usually insufficient for an investor-state tribunal to extend its jurisdiction over counterclaims.

C. CONTRACTS AS A SOURCE OF INVESTOR OBLIGATIONS

Most investor-state disputes involve one or more contracts concluded between the foreign investor and the State. That could be a privatization contract, a concession contract, a license agreement, or other types of contract. Unlike investment treaties, these contracts also include concrete investor obligations in addition to obligations of States. It is important to understand whether obligations of investors arising out of contracts can fall under the jurisdiction of investor-state tribunals.

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150. *Id.* ¶ 695.

151. *See, e.g.*, Spyridon Roussalis v. Romania, ICSID Case No. ARB/06/1, Award, ¶ 489 (Dec. 7, 2011), http://icsid.worldbank.org/ICSID/FrontServlet?requestType=CasesRH&actionVal=showDoc&docId=DC2431_En&caseId=C70; El Paso Energy International Co. v. Argentine Republic, ICSID Case No. ARB/03/15, Decision on Jurisdiction, ¶ 97 (Apr. 27, 2006), 21 ICSID Rev. 488 (2006). For a UNCITRAL dispute, see GAMI Investments, Inc. v. Mexico, Final Award, ¶¶ 26–43 (Nov. 15, 2004), 44 I.L.M. 545 (2005).

152. *See, e.g.*, *Spyridon Roussalis*, ICSID Case No. ARB/06/1 ¶ 490; *El Paso Energy International Co.*, 21 ICSID Rev. ¶ 97.

UNCITRAL and ICC arbitration rules provide that contract provisions should be taken into account when tribunals resolve disputes.[153] The reason why most arbitration rules explicitly cover contractual obligations is that those rules were originally developed for resolution of purely contractual disputes between private parties. Even the ICSID Convention was adopted primarily with contractual disputes in mind—when the Convention was finalized in 1965, there were almost no investment treaties.[154] On the other hand, nothing in Article 46 of the ICSID Convention implies that its purpose was only to encompass contractual disputes and to exclude investment treaty arbitrations.[155]

But it would be wrong to conclude that any obligations in contracts concluded between the foreign investor and the host State automatically rise to the level of being arbitrable by investor-state tribunals. As James Crawford suggested, contractual jurisdiction can be invoked under any sufficiently broad investment treaty dispute resolution clause as long as three conditions are met.[156] First, the contract should relate to an investment rather than being an ordinary contract for the supply of goods or services.[157] Second, the contract should be with the State itself and not with a separate legal entity controlled by the State or a third party.[158] Third, the contract with the State should not have its own dispute resolution clause.[159]

The same logic applies to counterclaims. States can assert counterclaims arising out of investor contractual obligations if there is a sufficiently broad investment treaty clause, and the investment contract with the State does not have its own dispute resolution mechanism.[160] For instance, the *Saluka v.*

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153. UNCITRAL Arbitration Rules, *supra* note 13, art. 35.3; ICC ARBITRATION RULES, *supra* note 13, art. 17.2.

154. *See* RUDOLF DOLZER & MARGRETE STEVENS, BILATERAL INVESTMENT TREATIES 1–10, 81–83, 129–30, 144–45 (1995).

155. Lalive & Halonen, *supra* note 11, at 143.

156. James Crawford, Whewell Professor of Int'l Law, Univ. of Cambridge, Freshfields Lecture on Treaty and Contract in Investment Arbitration, 13 (Nov. 29, 2007), *available at* http://www.lcil.cam.ac.uk/Media/lectures/pdf/Freshfields%20Lecture%202007.pdf.

157. *Id.*

158. *Id.*

159. *Id.*

160. *See, e.g.*, Saluka Investments BV v. Czech Republic, UNCITRAL, Decision on Jurisdiction over Czech Republic's Counterclaim, ¶¶ 37–39, 55–57 (May 7, 2004), 15 ICSID Rep. 256 (2010).

Czech Republic tribunal rejected jurisdiction over counterclaims arising from the Share Purchase Agreement because the agreement contained a separate dispute resolution clause.[161]

Subject matter jurisdiction of ICSID tribunals widens when treaty provisions guarantee the host State's observance of all obligations or commitments entered into *vis-à-vis* foreign investors. These provisions are commonly known as umbrella clauses.[162] Umbrella clauses are often referred to as *pacta sunt servanda* clauses because their purpose is to ensure that contracts are respected.[163] A typical umbrella clause provides that: "Each party shall observe any obligation it may have entered into with regard to investments."[164] According to Elihu Lauterpacht, the effect of umbrella clauses is to "put [investor-state contracts] on a special plane in that breach of them becomes immediately a breach of convention."[165]

The precise nature and effect of umbrella clauses is uncertain. Some commentators interpret them as protecting "the investor's contractual rights against any interference which might be caused by either a simple breach of contract or by administrative or legislative acts."[166] The application of this principle, however, does not explain whether umbrella clauses also cover purely commercial contracts.[167] Some tribunals consider these clauses as automatically elevating the host State's breaches of contract with investors to a treaty violation.[168] Other tribunals rejected this interpretation without

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161. *Id.* ¶¶ 55–57.

162. *See* Jarrod Wong, *Umbrella Clauses in Bilateral Investment Treaties: Of Breaches of Contract, Treaty Violations, and the Divide between Developing and Developed Countries in Foreign Investment Disputes*, 14 GEO. MASON L. REV. 135, 142–50 (2006).

163. *See id.* at 142–43.

164. Treaty Concerning the Reciprocal Encouragement and Protection of Investment, *supra* note 7, 31 I.L.M. at 130.

165. Elihu Lauterpacht, *The Drafting of Treaties for the Protection of Investment*, *in* THE ENCOURAGEMENT AND PROTECTION OF INVESTMENT IN DEVELOPING COUNTRIES 18, 31 (1962).

166. DOLZER & STEVENS, supra note 154, at 81–82.

167. U.N. Conference in Investment Rulemaking, at 74, UNCTAD/ITE/IIT/2006/5, U.N on Trade and Dev., Bilateral Investment Treaties 1995-2006: Trends. Sales No. E.06.II.D.16 (2007).

168. *See, e.g.*, Société Générale de Surveillance S.A. v. Republic of the Philippines, ICSID Case No. ARB/02/6, Decision on Objections to Jurisdiction, ¶¶ 113–29 (Jan. 29, 2004), 8 ISCID Rep. 518 (2005); Noble Ventures, Inc. v. Romania, ICSID Case No. ARB/01/11, Award, ¶¶ 46–62 (Oct. 12, 2005), http://italaw.com/documents/Noble.pdf.

explaining the meaning of the umbrella clauses.[169]

In the context of counterclaims, reliance on umbrella clauses to create investor obligations is problematic for another reason. Investment treaties usually provide that "Parties" (that is, States) should comply with their commitments.[170] Thus, in a strict sense umbrella clauses are not intended to impose any obligations on investors, only on States.

To summarize, purely contractual investor obligations do not fall under the jurisdiction of investor-state tribunals. The State, however, may assert counterclaims under a sufficiently broad investment treaty clause if the investor breached its obligations under the investment contract concluded with the State.

D. INTERNATIONAL LAW

a. Relevant Sources of International Law

As discussed above, investment treaties often provide that domestic law and international law govern disputes between the State and the investor.[171] In some cases, only international law governs substantive rights and obligations—for instance, the North American Free Trade Agreement[172] and the Energy Charter Treaty[173] provide for international law as the sole source of the applicable law.

A number of ICSID tribunals have explained that international law remains applicable in ICSID proceedings unless the parties have specifically excluded its application.[174] If domestic law is chosen as applicable, international law plays a supplemental and corrective function.[175] This means that international law fills the gaps in the host State's laws, and if

169. *See, e.g.*, Société Générale de Surveillance S.A. v. Islamic Republic of Pakistan, ICSID Case No. ARB/01/13, Decision on Objections to Jurisdiction, ¶¶ 163–74 (Aug. 6, 2003), 8 ICSID Rep. 406 (2005).

170. Treaty Concerning the Reciprocal Encouragement and Protection of Investment, *supra* note 7, 31 I.L.M. at 130.

171. *See* BEGIC, *supra* note 131, at 232.

172. NAFTA, *supra* note 81, 32 I.L.M. at 645.

173. ECT, *supra* note 77, 34 I.L.M. at 400.

174. *See, e.g.*, MTD Equity Sdn. Bhd. v. Republic of Chile, ICSID Case No. ARB/01/7, Award, ¶¶ 86–87 (May 25, 2004), 12 ICSID Rep. 6 (2007); Southern Pacific Properties (Middle E.) Ltd. v. Arab Republic of Egypt, ICSID Case No. ARB/84/3, Award, ¶ 84 (May 20, 1992), 3 ICSID Rep. 189 (1995); Amco Asia Corp. et al. v. Republic of Indonesia, ICSID Case No. ARB/81/1, Resubmitted Case: Award, ¶¶ 37–40 (May 31, 1990), 1 ICSID Rep. 569 (1993).

175. DOCUMENTS CONCERNING THE ORIGIN AND THE FORMULATION OF THE CONVENTION, *supra* note 44, at 570–71, 985–86.

there is a conflict between international and domestic law, international law prevails.[176] This principle is consistent with the general rule of international law under which States are not allowed to rely on domestic law to avoid performing their obligations under treaties.[177]

According to the Report of ICSID Executive Directors, the term 'international law' has the same meaning as Article 38(1) of the Statute of the International Court of Justice (ICJ).[178] Article 38(1) provides a classical definition of sources of international law:

> international conventions, whether general or particular, establishing rules expressly recognized by the contesting states;
>
> international custom, as evidence of a general practice accepted as law;
>
> the general principles of law recognized by civilized nations;
>
> . . . judicial decisions and the teachings of the most highly qualified publicists of the various nations, as subsidiary means for the determination of rules of law.[179]

It is important to understand that parties in ICJ proceedings for which the ICJ Statute had been adopted are sovereign States.[180] Investor-state disputes are different because one party is not a sovereign. Therefore, general international law should be applied differently in the context of international investment law, which constitutes a self-contained legal regime.

According to international law theory, self-contained regimes are interrelated wholes of primary and secondary rules that cover some particular problem differently from the way it would be covered under general law.[181] Examples of self-

176. *See* BEGIC, *supra* note 131, at 155; Aaron Broches, *The Convention on the Settlement of Investment Disputes between States and Nationals of Other States*, 136 RECUEIL DES COURS 387–93 (1972).

177. Vienna Convention on the Law of Treaties, *supra* note 65, 1155 U.N.T.S. at 339 ("A party may not invoke the provisions of its internal law as justification for its failure to perform a treaty.").

178. Int'l Bank for Reconstruction and Dev., *Report of the Executive Directors on the Convention on the Settlement of Investment Disputes between States and Nationals of Other States* (Mar. 18, 1965), *compiled in ICSID Convention, Rules and Regulations*, at 47, ICSID/15 (Apr. 2006), *available at* http://icsid.worldbank.org/ICSID/StaticFiles/basicdoc/CRR_English-final.pdf.

179. Statute of the International Court of Justice, art. 38(1), June 26, 1945, 59 stat. 1055.

180. *Id.* art. 34(1).

181. *See generally* Rep. of the Int'l Law Comm'n, *Fragmentation of International Law: Difficulties Arising from the Diversification*

contained regimes include WTO law or the law of diplomatic protection.[182] A self-contained regime (*lex specialis*) provides interpretative guidance that in some ways deviates from the rules of general law (*lex generalis*).[183]

As the Iran-US Claims Tribunal explained in *Amoco v Iran*:

> As a *lex specialis* in relations between the two countries, the Treaty supersedes the *lex generalis*, namely customary international law . . . however . . . the rules of customary international law may be useful in order to fill in possible *lacunae* of the Treaty, to ascertain the meaning of undefined terms in its text or, more generally, to aid interpretation and implementation of its provisions.[184]

In the past, investor-state tribunals applied treaties, customary international law, and general principles of law in addition to investment treaties to determine the obligations of the parties.[185] As the analysis below suggests, not all of these sources of international law help determine investor obligations.

b. International Conventions

International conventions, and in particular investment treaties, are the first and foremost source of international law applied by investor-state tribunals. In addition to investment treaties, multilateral treaties such as NAFTA and ECT contain provisions for arbitration of investor-state disputes.[186] They provide specific rights of foreign investors such as protection against expropriation and the right to fair and equitable treatment.[187]

It is not surprising that while treaties provide for investor rights, investor obligations are not there. Investors cannot be parties to international treaties concluded by States. Can

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and Expansion of International Law: Rep. of the Study Grp. of the Int'l Law Comm'n, 58th sess., May 1–June 9, July 3–Aug. 11, 2006, U.N. Doc. A/CN.4/L.682, 68 (Apr. 13, 2006) (finalized by Martti Koskenniemi).

182. *Id.* at 65–69.

183. *Id.* at 70.

184. Amoco International Finance Corp. v. Iran, ¶ 112, 15 Iran-U.S. Cl. Trib. Rep. 189 (1987).

185. Ole Kristian Fauchald, *The Legal Reasoning of ICSID Tribunals – An Empirical Analysis*, 19 EUR. J. OF INT'L L. 301, 309–14, 328–33 (2008).

186. ECT, *supra* note 77, 34 I.L.M. at 399–401; NAFTA, *supra* note 81, 32 I.L.M. at 642–47.

187. ECT, *supra* note 77, 34 I.L.M. at 363; NAFTA, *supra* note 81, 32 I.L.M. at 639–42.

treaties, in principle, impose obligations on investors who are not parties to them? If treaties were treated as regular contracts, then no obligations could be imposed on third parties, only rights. According to a universally accepted principle of contract law, a third party cannot be subjected to a burden by a contract to which it is not a party.[188]

A number of developing countries advocate for inclusion of investor obligations directly in international investment agreements. In 2002, China, Cuba, India, Kenya, Pakistan, and Zimbabwe proposed that discussions on a multilateral framework on trade and investment also look at legally binding measures aimed at ensuring corporate responsibility and accountability relating to foreign investors.[189] In particular, they insisted on the need to comply with all domestic laws and regulations in all aspects of the economic and social lives of the host States in their activities.[190]

Investors, however, are already required to abide by domestic laws of the State in which they operate.

This is a consequence not only of domestic law requirements, but also of the international law principle of territorial sovereignty.[191] The host State, as a sovereign actor, can react to investor misconduct by unilaterally imposing sanctions and enforcing them against the assets of the investment project.[192] This is a power the host State already possesses and that the foreign investor lacks.[193] Although this principle is sometimes spelled out in international agreements,[194] it applies by virtue of public international law in

188. EWAN MCKENDRICK, CONTRACT LAW 133 (Marise Cremona ed., 4th ed. 2000).

189. *See* Working Group on the Relationship between Trade and Investment, *Communication from China, Cuba, India, Kenya, Pakistan and Zimbabwe: Investors' and Home Governments' Obligations*, WT/WGTI/W/152 (*received* Nov. 19, 2002).

190. *See id.*

191. *See generally* BROWNLIE, *supra* note 98, at 105–07 (explaining the concepts of territory, sovereignty, and territorial sovereignty).

192. *See generally* Organisation for Economic Co-operation and Development, *"Indirect Expropriation" and the "Right to Regulate" in International Investment Law*, Working Papers on International Investment Number 2004/4 (Sept. 2004), *available at* www.oecd.org/dataoecd/22/54/33776546.pdf (discussing how the scope of a host State's power to regulate the rights and obligations of investors is determined).

193. *See* Brower & Schill, *supra* note 6, at 482. There are also situations in which investors do not keep sufficient assets in the host States which prevents this mechanism from working effectively.

194. Association of Southeast Asian Nations, *Framework Agreement on the*

any event.[195]

Because investment and other treaties usually do not provide for specific investor obligations, such obligations should be looked for in other primary and secondary sources of international law such as international custom and general principles of law.

c. International Custom

If investor obligations are not set out in relevant treaties, or if their provisions are not sufficiently complete, the tribunal may refer to international custom unless the treaty refers to the application of different law (for example, domestic law).[196]

For instance, in *ADC v. Hungary*, the tribunal first applied the relevant investment treaty and then explained that consent to arbitration

> must also be deemed to comprise a choice for general international law, including customary international law, if and to the extent that it comes into play for interpreting and applying the provisions of the Treaty.[197]

According to Article 38 of the ICJ Statute, international custom constitutes "evidence of a general practice accepted as law."[198] The definition includes two basic elements—the actual behavior of States, and the psychological or subjective belief that such behavior is law.[199]

The ICSID Convention drafters discussed a number of rules of customary international law. These rules included the obligation to act in good faith,[200] protection against

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ASEAN Investment Area, art. 13 (Oct. 7, 1998) (allowing Member States to undertake any measures necessary to protect national security, public morals, the prevention of fraud or deceptive practices, and to ensure compliance with their tax obligations in the host jurisdiction).

195. *See id.*

196. Article 38(1) of the ICJ Statute, *supra* note 179.

197. ADC Affiliate Ltd. v. Republic of Hungary, ICSID Case No. ARB/03/16, Award, ¶ 290 (Oct. 2, 2006), 15 ICSID Rep. 534; *see also* Siemens AG v. Argentine Republic, ICSID Case No. ARB/02/8, Award, ¶ 349 (Feb. 6, 2007), 14 ICSID Rep. 518 (2009) (looking at customary international law to determine the standard of compensation for unlawful expropriation).

198. Statute of the International Court of Justice art. 38, June 26, 1945, 59 Stat. 1055, 1060.

199. Rajendra Ramlogan, *The Environment and International Law: Rethinking the Traditional Approach*, 3 VT. J. ENVTL. L. 1, 3 (2001–2002).

200. Regional Consultative Meetings of Legal Experts on Settlement of Investment Disputes, *Chairman's Report on Issues Raised and Suggestions Made With Respect to the Preliminary Draft of a Convention on the Settlement of Investment Disputes Between States and Nationals of Other States*, art. IV, ¶ 59, Z11 (July 9, 1964), *in* 2 INTERNATIONAL CENTER FOR SETTLEMENT OF

discriminatory treatment,[201] the prohibition of measures contrary to international public policy,[202] *pacta sunt servanda*,[203] the exhaustion of local remedies,[204] and rules on State succession.[205] The ICSID Convention, however, mentions none of these principles. Moreover, it is difficult to apply these principles to investor conduct because they deal primarily with conduct of States rather than private parties such as investors.

Do the most important rules of international customary law, known as *jus cogens* norms[206] (for example, prohibition of genocide, slavery), affect obligations of investors? That would be problematic because only States (and individuals under certain circumstances), but not corporations, are responsible under international law for violations of such norms.[207] Moreover, corporate criminal liability generally exists neither in international law nor in the majority of domestic legal systems.[208]

The main problem in applying customary international law is that it develops as a result of interaction between States and is meant to create obligations for States,[209] not private investors. Customary international law affects interpretations

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INVESTMENT DISPUTES, DOCUMENTS CONCERNING THE ORIGIN AND THE FORMULATION OF THE CONVENTION, 557 (International Center for Settlement of Investment Disputes, Washington, D.C., 1968).

201. *See* Settlement of Investment Disputes Consultative Meeting of Legal Experts, *Summary Record of Proceedings*, art. IV, at 51, Z9 (June 1, 1964), *in* 2 INTERNATIONAL CENTER FOR SETTLEMENT OF INVESTMENT DISPUTES, DOCUMENTS CONCERNING THE ORIGIN AND THE FORMULATION OF THE CONVENTION, 367 (International Center for Settlement of Investment Disputes, Washington, D.C., 1968).

202. *See* Legal Committee on Settlement of Investment Disputes, *Summary Proceedings of the Legal Committee Meeting*, SID/LC/SR/14, art. 44, at 3 (Dec. 30, 1964) *in* 2 INTERNATIONAL CENTER FOR SETTLEMENT OF INVESTMENT DISPUTES, DOCUMENTS CONCERNING THE ORIGIN AND THE FORMULATION OF THE CONVENTION, 799 (International Center for Settlement of Investment Disputes, Washington, D.C., 1968).

203. *See id.*

204. *See id.*

205. *See id.*

206. Vienna Convention on the Law of Treaties, *supra* note 65, art. 53 ("[A] peremptory norm of general international law is a norm accepted and recognized by the international community of States as a whole as a norm from which no derogation is permitted and which can be modified only by a subsequent norm of general international law having the same character.").

207. *See, e.g.,* The I.G. Farben Trial, Case No. 57, The Judgment of the Tribunal X L. REP. TRIALS WAR CRIMS. 30, 52 (1948).

208. ILIAS BANTEKAS & SUSAN NASH, INTERNATIONAL CRIMINAL LAW 47 (3rd ed. 2007).

209. *See* BROWNLIE, *supra* note 98, at 6–12.

of treaties and obligations of one State *vis-à-vis* another but does not directly create obligations of investors. On the other hand, general principles of law are helpful for determining obligations of non-State actors such as investors as discussed below.

d. General Principles of Law

General principles of law have played a prominent role in arbitrations between States and foreign nationals,[210] as the jurisprudence of the IUSCT and ICSID cases demonstrates. General principles of law can come from comparative municipal law, the *lex mercatoria*, and public international law.[211]

Choosing domestic law as applicable does not make general principles of law irrelevant. The sole arbitrator in a non-ICSID investor-state dispute in *Texaco v. Libya* explained the relevance of general principles of law when domestic Libyan law was chosen as applicable. The arbitrator provided that:

> [T]he application of the principles of Libyan [domestic] law does not have the effect of ruling out the application of the principles of international law, but quite the contrary: it simply requires us to combine the two in verifying the conformity of the first with the second.[212]

The arbitrator relied both on the principle of the binding force of contracts recognized by Libyan law and on the principle *pacta sunt servanda* (agreements must be kept), which is essential to international law.[213]

The United Nations Charter recognizes the importance of the principle of good faith.[214] This principle comes into play in the context of the exercise of rights by States[215] and is otherwise

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210. Richard B. Lillich, *The Law Governing Disputes under Economic Development Agreements: Reexamining the Concept of "Internalization," in* INTERNATIONAL ARBITRATION IN THE 21ST CENTURY: TOWARDS "JUDICIALIZATION" AND UNIFORMITY? 61, 107–10 (Richard B. Lillich & Charles N. Brower eds., 1993); K. Lipstein, *International Arbitration Between Individuals and Governments and the Conflict of Laws, in* CONTEMPORARY PROBLEMS OF INTERNATIONAL LAW: ESSAYS IN HONOUR OF GEORGE SCHWARZENBERGER ON HIS EIGHTIETH BIRTHDAY 177 (Bin Cheng & E. D. Brown eds., 1988).

211. Grant Hanessian, *"General Principles of Law" in the Iran-U.S. Claims Tribunal*, 27 COLUM. J. TRANSNAT'L L. 309, 318 (1988).

212. Texaco Overseas Petroleum Co./Cal. Asiatic Oil Co. v. Government of the Libyan Arab Republic, Award, ¶ 49 (Jan. 19, 1977), 17 I.L.M. 1 (1978).

213. *See id.* ¶ 51.

214. *See* U.N. Charter art. 2, para. 2.

215. BIN CHENG, GENERAL PRINCIPLES OF LAW AS APPLIED BY INTERNATIONAL COURTS AND TRIBUNALS 121 (George W. Keeton & Georg

described as the prohibition of malicious injury, that is, the exercise of a right—or supposed right—for the sole purpose of causing injury to another.[216]

The principle of good faith establishes interdependence between the rights of an investor and its obligations. A bona fide exercise of a right is expected rather than an exercise aimed at procuring an unfair advantage.[217] The exercise of a right in a manner which prejudices the interests of the other party (the State) would constitute a breach of the principle.[218]

International arbitration tribunals have developed increasingly specialized general principles of law in their case law.[219] The general principle of good faith gives rise to more specific obligations such as good faith in the conclusion, interpretation, and performance of contracts.[220] An even more specific principle would be interpretation against a party that unilaterally drafted a contract.[221]

Other examples of general principles of law applied by investor-state tribunals include *restitutio in integrum*[222] and an injured person's duty to mitigate damages.[223] Tribunals have also applied principles of *pacta sunt servanda*,[224] estoppel,[225]

Schwarzenberger eds., 1953). For an application of the principle in an ICSID context, see Inceysa Vallisoletana, S.L. v. Republic of El Salvador, ICSID Case No. ARB/03/26, Award, ¶¶ 230–39 (Aug. 2, 2006), http://italaw.com/documents/Inceysa_Vallisoletana_en_001.pdf.

216. *See* CHENG, *supra* note 215, at 122. For an application of this principle in an investor-state context, see Saipem S.p.A. v. People's Republic of Bangladesh, ICSID Case No. ARB/05/07, Decision on Jurisdiction and Recommendation on Provisional Measures, ¶¶ 154–58 (Mar. 21, 2007), 22 ICSID Rev. 100 (2007). *See also* Waguih Elie George Siag v. Arab Republic of Egypt, ICSID Case No. ARB/05/15, Decision on Jurisdiction, ¶ 213 (Apr. 11, 2007), http://italaw.com/documents/Siagv.Egypt.pdf.

217. *See* CHENG, *supra* note 215, at 125.

218. *Id.*

219. *See* EMMANUEL GAILLARD, LEGAL THEORY OF INTERNATIONAL ARBITRATION 54 (2010).

220. *Id.*

221. *Id.*

222. *See* Texaco Overseas Petroleum Co./Cal. Asiatic Oil Co. v. Government of the Libyan Arab Republic, Award, ¶¶ 97–109 (Jan. 19, 1977), 17 I.L.M. 1 (1978); *see also* Amco Asia Corp. et al. v. Republic of Indonesia, ICSID Case No. ARB/81/1, Award, ¶ 268 (Nov. 20, 1984), 1 ICSID Rep. 413 (1993).

223. *See* Middle E. Cement Shipping and Handling Co. v. Arab Republic of Egypt, ICSID Case No. ARB/99/6, Award, ¶ 167 (Apr. 12, 2002), 7 ICSID Rep. 173 (2005).

224. *See Texaco Overseas Petroleum Co.*, 17 I.L.M. ¶ 51.

225. *See* S. Pac. Props. (Middle E.) Ltd. v. Arab Republic of Egypt, ICSID Case No. ARB/84/3, Award, ¶ 247 (May 20, 1992), 3 ICSID Rep. 102 (1995); *see*

nemo auditur propriam turpitudinem allegans (prohibition from benefiting from one's own fraud),[226] *exceptio non adimpleti contractus* (person who is being sued for non-performance of contractual obligations can defend themselves by proving that the plaintiff did not perform their side of the bargain),[227] unjust enrichment,[228] and general principles of contract law.[229]

Unlike international treaties or international customary law, general principles of law can provide for obligations of private parties. In the absence of specific provisions setting out obligations of investors in international treaties, these principles of law serve as an appropriate source of law to determine obligations of investors in investor-state arbitration.

e. Jurisprudence and Scholarly Writings

While some general principles of law and legal rules are codified and easy to access,[230] other principles are more difficult to identify.[231] In practice, tribunals often skip the process of finding the "general principles of law recognized by civilized nations" mentioned in Article 28 of the ICJ Statute because it is difficult and time-consuming. Instead, tribunals tend to rely on relevant international jurisprudence.[232]

International law does not operate on the basis of *stare decisis* or prior ICSID awards. Even prior ICSID awards applying similar investment treaty language do not constitute

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also Klöckner Industrie-Anlagen GmbH v. Republic of Cameroon, ICSID Case No. ARB/81/2, Decision on Annulment, ¶ 123 (May 3, 1985), 2 ICSID Rep. 3 (1994).

226. *See* Inceysa Vallisoletana, S.L. v. Republic of El Salvador, ICSID Case No. ARB/03/26, Award, ¶¶ 240–44 (Aug. 2, 2006), http://italaw.com/documents/Inceysa_Vallisoletana_en_001.pdf.

227. *See* Klöckner Industrie-Anlagen GmbH v. Republic of Cameroon, ICSID Case No. ARB/81/2, Award, 61–72 (Oct. 21, 1983), 2 ICSID Rep. 3 (1994); Autopista Concesionada de Venezuela CA v. Bolivarian Republic of Venezuela, ICSID Case No. ARB/00/5, Award, ¶ 316, (Sept. 23, 2003), 10 ICSID Rep. 309 (2006).

228. *See* Amco Asia Corp. et al. v. Republic of Indonesia, ICSID Case No. ARB/81/1, Resubmitted Case: Award, ¶¶ 154–56 (June 5, 1990), 1 ICSID Rep. 569 (1993); *S. Pac. Props. (Middle E.) Ltd.*, 3 ICSID Rep. ¶¶ 245–49; *Inceysa Vallisoletana, S.L.*, ICSID Case No. ARB/03/26 ¶¶ 253–57.

229. *See* Amco Asia Corp. et al. v. Republic of Indonesia, Award, ¶¶ 180–83 (Nov. 20, 1984), 1 ICSID Rep. 413 (1993).

230. International Institute for the Unification of Private Law, UNIDROIT Principles of International Commercial Contracts 2004 (International Institute for the Unification of Private Law, Rome, 2004).

231. General principles of law often overlap with other sources of international law. *See* BROWNLIE, *supra* note 98, at 19.

232. *See* Fauchald, *supra* note 185, at 309–13.

binding precedent.[233] Many investor-state tribunals, however, found themselves not barred, as a matter of principle, from considering the position taken or the opinion expressed by other tribunals.[234]

An ICSID tribunal in *ADC v. Hungary* emphasized, despite their non-binding nature, that

> cautious reliance on certain principles developed [in case law], as persuasive authority, may advance the body of law, which in turn may serve predictability in the interest of both investors and host States.[235]

In addition to case law, investor-state tribunals often rely on scholarly writings to help establish norms of law.[236]

Therefore, international jurisprudence and scholarly writings can be used as subsidiary means of identifying investor obligations in investor-state disputes.

V. CONCLUSION

The growing number of counterclaims submitted by States goes hand in hand with the growing number of investor-state disputes. The 2010 revision of the UNCITRAL Arbitration Rules, which broadened jurisdiction of UNCITRAL tribunals, will further increase the number of State counterclaims. Correct understanding of the mechanism of investor consent to counterclaims and correct identification of investor obligations will make the system of investor-state dispute resolution more efficient and fair.

Investor consent to counterclaims is essential. The relevant treaty dispute resolution clause affects jurisdiction of investor-state tribunals. If the treaty contains an offer of jurisdiction only in relation to disputes arising out of State obligations, it may be difficult for the tribunal to extend its jurisdiction over counterclaims unless the parties subsequently alter this offer by an explicit or implicit agreement.

Identification of investor obligations is crucial to

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233. *See* AES Corp. v. Argentine Republic, ICSID Case No. ARB/02/17, Decision on Jurisdiction, ¶¶ 27–28 (Apr. 26, 2005), 12 ICSID Rep. 308 (2007) (noting that although the tribunal may choose to follow positions taken by other tribunals, it is not required to do so).

234. *Id.*

235. ADC Affiliate Ltd. v. Republic of Hungary, ICSID Case No. ARB/03/16, Award, ¶ 293 (Oct. 2, 2006), 15 ICSID Rep. 534 (2010).

236. For a survey of sources relied upon by investor-state tribunals, see Jeffrey Commission, *Precedent in Investment Treaty Arbitration: A Citation Analysis of a Developing Jurisprudence*, 24 J. INT'L ARB. 129 (2007).

determining the substantive content of the procedural right to counterclaim. Although investment treaties usually do not provide for investor obligations, such obligations can be found in other sources of law.

Counterclaims cannot be based on domestic law obligations of investors unless such obligations were specifically mentioned in the relevant investment treaty or otherwise violate the parties' preexisting international law commitments. Otherwise, violation of purely domestic law obligations is insufficient for an investor-state tribunal to extend its jurisdiction over counterclaims.

In the absence of concrete provisions setting out investor obligations in international treaties, general principles of law appear to be an appropriate source of international law to determine such obligations.

Contractual obligations of investors fall outside of the jurisdiction of investor-state tribunals with one exception. The State may assert counterclaims if the investor breached its obligations under the investment contract concluded with the State provided that the relevant investment treaty or an arbitration agreement contains a sufficiently broad dispute resolution clause.