

STATE COUNTERCLAIMS IN INVESTOR-STATE  
DISPUTES: A HISTORY  
OF 30 YEARS OF FAILURE\*

*LAS CONTRADEMANDAS  
EN CONTROVERSIAS INVERSIONISTA-ESTADO:  
30 AÑOS DE FRACASOS*

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## ABSTRACT

Investor-State forums, particularly ICSID, permit and encourage State counterclaims. Yet State counterclaims in investor-State disputes always fail. This article surveys State counterclaims in investor-State disputes in an attempt to understand why they always fail. The article first examines jurisdictional requirements for State counterclaims. Subsequently, the article summarizes and aggregates tribunals' interpretations of these requirements, extracting a rough representation of counterclaim treatment. Cumulative information suggests that the repeated failures might be explained in part by narrow interpretations of counterclaim jurisdictional requirements. As well, lack of substantive protections for States in bilateral investment treaties, free trade agreements and other international investment agreements (IIAs) appears to exacerbate the problem. Finally, the article suggests that concerned States include substantive protections for States in their IIAs.

**Key words author:** State Counterclaims, Jurisdictional Requirements, ICSID Convention, International Investment Agreements.

**Key words plus:** Counterclaims, International Centre for Settlement of Investment Disputes, Court rules.

**RESUMEN**

*Los foros para la solución de Controversias Inversionista-Estado, particularmente el CIADI, permiten y promueven las contrademandas por parte de los Estados. Sin embargo, las contrademandas en controversias inversionista-Estado nunca prosperan. El presente artículo investiga y analiza las razones por las cuales las contrademandas en controversias inversionista-Estado no prosperan. En primer lugar, el artículo examina los requisitos jurisdiccionales para la presentación de contrademandas por parte de los Estados. Posteriormente, el artículo resume y agrega las interpretaciones de los tribunales inversionista-Estado con respecto a estos requisitos jurisdiccionales y describe un panorama general sobre su entendimiento. La información recopilada sugiere, en parte, que las contrademandas no prosperan debido a una interpretación restrictiva de los requisitos jurisdiccionales. Adicionalmente, la ausencia de estándares de protección a favor de los Estados en tratados bilaterales de inversión (TBI), tratados de libre comercio y otros acuerdos internacionales de inversión ayuda a agravar el problema. Por último, el artículo concluye y sugiere que los Estados deben empezar a incluir estándares de protección a su favor en los acuerdos internacionales de inversión.*

**Palabras clave autor:** *Contrademandas, requisitos jurisdiccionales, Convención del CIADI, Acuerdos Internacionales de Inversión, AII.*

**Palabras clave descriptor:** *Demanda de reconvencción, Centro Internacional de Arreglo de Diferencias Relativas a Inversiones, reglamentos de tribunales.*

**SUMMARY**

INTRODUCTION.- I. THE PROBLEM.- II. STATES' RIGHT TO COUNTERCLAIM.- A. "Within the scope of consent of the parties".- B. Arising out of "the subject matter" and "an investment".- III. ICSID JURISDICTIONAL REQUIREMENTS.- IV. CASES.- A. Contract-Based Claims.- 1. Early Counterclaims.- 2. Cases Limiting Jurisdiction and Substantive Protections.- 3. Cases Reducing Awards.- B. State Counterclaims under an IIA.- 1. Finding jurisdiction under a BIT.- 2. Tribunal willingness.- 3. Suggested solution.- V. CURRENT DETERRENCE ALTERNATIVES.- VI. CONCLUSION.- BIBLIOGRAPHY.

## INTRODUCTION

This article outlines State counterclaims in investor-State disputes, focusing primarily on claims brought before the International Center for Settlement of Investment Disputes (ICSID). The article opens, in Part I, by highlighting the current imbalance between State and investor rights in investor-State disputes. Part II points out that this imbalance departs from the ICSID drafters' vision. Part III then examines ICSID jurisdictional requirements for State counterclaims. Part IV looks at how tribunals have interpreted these requirements. This section is divided into two. Part IV(A) surveys claims arising from investment agreements between the State and the investor. Part IV(B) examines counterclaims arising from investment treaties. Finally, Part V quickly outlines alternative courses of action that tribunals are taking to address this problem.

## I. THE PROBLEM

ICSID explicitly provides jurisdiction for State counterclaims and claims. Yet, in all of its 30 years only about 20 States have counterclaimed.<sup>1</sup> ICSID was created to foster “international cooperation for economic development.”<sup>2</sup> So it is understandable that ICSID is currently a forum for investors to bring claims against States. ICSID, however, was conceived as a forum for States to bring claims against investors as well. “*The provisions of the Convention maintain a careful balance between the interests of investors and those of host States. Moreover, the Convention permits the institution of proceedings by host States as well as by investors.*”<sup>3</sup>

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1 Most of these cases are mentioned in this article.

2 Convention on the Settlement of Investment Disputes between States and Nationals of Other States (as amended April 10<sup>th</sup>, 2006), art. 46, March 18<sup>th</sup>, 1965. Convention on the Settlement of Investment Disputes between States and Nationals of other States (as amended April 10<sup>th</sup>, 2006), *ICSID Rules and Regulations* (March 18<sup>th</sup>, 1965). <http://icsid.worldbank.org/ICSID/ICSID/RulesMain.jsp>.

3 Report of the Executive Directors of the International Bank for Reconstruction and Development on the Convention on the Settlement of Investment Disputes between States

The evolution of the system for international investment has transformed this broadly conceived forum into a relatively unilateral forum. Under the current system, the best a Respondent State can hope for is that the investor covers their legal costs. As a result, investors have much to gain, and States everything to lose.

Successful State counterclaims and claims, where merited, might serve to deter frivolous claims and provide respondent States with motive to bypass jurisdictional objections and move straight to the merits.

## II. STATES' RIGHT TO COUNTERCLAIM

ICSID not only permits, but encourages counterclaims and State claimants. The drafters envisioned the Centre as a multidimensional forum. Every provision of the Convention treats consenting States and consenting investors equally. The only inherent points of difference, then, are investor consent and any distinction housed within an applicable BIT or contract.

Article 46 of the ICSID Convention states, “*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.*”<sup>4</sup>

The Report of Executive Directors goes further, encouraging counterclaims and State-initiated claims, even advocating differentiation to ensure equality.

*While the broad objective of the Convention is to encourage a larger flow of private international investment, the provisions of the Convention maintain a careful balance between the interests of investors and those of host States.*

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and Nationals of Other States (as amended April 10<sup>th</sup>, 2006) [ICSID Convention], March 18<sup>th</sup>, 1965. <http://icsid.worldbank.org/ICSID/ICSID/RulesMain.jsp>.

4 Convention on the Settlement of Investment Disputes between States and Nationals of other States, art. 46 (as amended April 10<sup>th</sup>, 2006), *ICSID Rules and Regulations* (March 18<sup>th</sup>, 1965. <http://icsid.worldbank.org/ICSID/ICSID/RulesMain.jsp>).

*Moreover, 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.*<sup>5</sup>

Likewise, the Preamble and other clauses provide equal rights to investors and States. The Preamble sets forth the premise of the Convention. “*Considering the need for international cooperation for economic development, and the role of private international investment therein; Bearing in mind the possibility that from time to time disputes may arise in connection with such investment between Contracting States and nationals of other Contracting States.*”<sup>6</sup> Nothing in the preamble implies differential access to ICSID procedures.

The Centre's “*purpose*” also treats the two equally. The purpose “*shall be to provide facilities for conciliation and arbitration of investment disputes between Contracting States and nationals of other Contracting States in accordance with the provisions of this Convention.*”<sup>7</sup> Indeed, Article 36 invites both States and nationals to institute proceedings assuming consent is given, and lists the State first. “*(1) Any Contracting State or any national of a Contracting State wishing to institute arbitration proceedings shall address a request to that effect in writing to the Secretary-General who shall send a copy of the request to the other party.*”<sup>8</sup>

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5 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 (as amended April 10<sup>th</sup>, 2006) [ICSID Convention], March 18<sup>th</sup>, 1965. <http://icsid.worldbank.org/ICSID/ICSID/RulesMain.jsp>.

6 Convention on the Settlement of Investment Disputes between States and Nationals of other States, Preamble (as amended April 10<sup>th</sup>, 2006), *ICSID Rules and Regulations* (March 18<sup>th</sup>, 1965). <http://icsid.worldbank.org/ICSID/ICSID/RulesMain.jsp>.

7 Convention on the Settlement of Investment Disputes between States and Nationals of other States, art. 1.2, (as amended April 10<sup>th</sup>, 2006), *ICSID Rules and Regulations* (March 18<sup>th</sup>, 1965). <http://icsid.worldbank.org/ICSID/ICSID/RulesMain.jsp>.

8 Convention on the Settlement of Investment Disputes between States and Nationals of other States, art. 36 (as amended April 10<sup>th</sup>, 2006), *ICSID Rules and Regulations* (March 18<sup>th</sup>, 1965). <http://icsid.worldbank.org/ICSID/ICSID/RulesMain.jsp>. See also, *id.*, art. 28: “*(1) Any Contracting State or any national of a Contracting State wishing to institute conciliation proceedings shall address a request to that effect in writing to the Secretary-General who shall send a copy of the request to the other party.*”

There is a clear emphasis on equality of access between States and investors. The current dynamic of investor-State disputes, however, seems to contradict the principle of equality. This may be partly explained by the evolution of jurisdictional interpretations, which leaves the State with limited access to ICSID and limited recourse to counterclaims. The other element limiting State counterclaims is the unilateral nature of current International Investment Agreements (IIAs), which provide substantive protections exclusively to investors.

### III. ICSID JURISDICTIONAL REQUIREMENTS

ICSID requirements are simple and open-ended. The investor must have consented to jurisdiction and the claim must arise directly out of the subject matter of the dispute (Article 46) and arise directly out of an investment (Article 25.1). Procedural Rule 40 provides some limits with respect to timing and filing of counterclaims.<sup>9</sup>

#### *A. Within the scope of consent of the parties*

ICSID jurisdiction requires consent. Article 25.1 requires that “*the parties to the dispute consent in writing to submit to the Centre.*”<sup>10</sup> It adds, “*When the parties have given their consent, no party may withdraw its consent unilaterally.*”<sup>11</sup> Article 46 requires

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9 International Centre for Settlement of Investment Disputes, ICSID, *Rules of Procedure for Arbitration Proceedings, ICSID Institution Rules* (as amended April 10<sup>th</sup>, 2006), (March 18<sup>th</sup>, 1965). <http://icsid.worldbank.org/ICSID/ICSID/RulesMain.jsp>.

International Centre for Settlement of Investment Disputes, ICSID, *Rules of Procedure for Arbitration Proceedings, ICSID Institution Rules*, art. 40 (as amended April 10<sup>th</sup>, 2006), (March 18<sup>th</sup>, 1965). <http://icsid.worldbank.org/ICSID/ICSID/RulesMain.jsp>.

10 Convention on the Settlement of Investment Disputes between States and Nationals of other States, art. 36 (as amended April 10<sup>th</sup>, 2006), *ICSID Rules and Regulations* (March 18<sup>th</sup>, 1965). <http://icsid.worldbank.org/ICSID/ICSID/RulesMain.jsp>.

11 Convention on the Settlement of Investment Disputes between States and Nationals of other States, art. 25.1 (as amended April 10<sup>th</sup>, 2006), *ICSID Rules and Regulations* (March 18<sup>th</sup>, 1965). <http://icsid.worldbank.org/ICSID/ICSID/RulesMain.jsp>.

that a counterclaim be “*within the scope of the consent of the parties.*”<sup>12</sup>

Article 46 does not explicitly impose any additional consent requirements. As a result, the only textual requirement is that the investor consent under Article 25.1, which may be done in a number of ways. *Executive Board Comment 24* provides some guidance.

*Consent may be given, for example, in a clause included in an investment agreement, providing for the submission to the Centre of future disputes arising out of that agreement, or in a compromis regarding a dispute which has already arisen. Nor does the Convention require that the consent of both parties be expressed in a single instrument. Thus, a host State might in its investment promotion legislation offer to submit disputes arising out of certain classes of investments to the jurisdiction of the Centre, and the investor might give his consent by accepting the offer in writing.*<sup>13</sup>

Specifically, it includes “*investment agreements*” and a “*compromis*” regarding already submitted disputes. Thus, a State clearly may initiate a claim against a company with which it has an investment agreement or once an investor makes a claim.

In general, investor consent is more difficult to locate since investors are not parties to IIAs – instruments that often constitute State consent. This presents a problem with respect to the ICSID Convention, as the Convention affirms a desire to balance State and investor rights. “[*T*]he provisions of the Convention should be equally adapted to the requirements of both cases.”<sup>14</sup>

Comment 24 contemplates a similarly flexible notion of consent. “*Nor does the Convention require that the consent of both parties be expressed in a single instrument.*”<sup>15</sup> In sum, the drafters understood

12 Convention on the Settlement of Investment Disputes between States and Nationals of other States, art. 46 (as amended April 10<sup>th</sup>, 2006), *ICSID Rules and Regulations* (March 18<sup>th</sup>, 1965). <http://icsid.worldbank.org/ICSID/ICSID/RulesMain.jsp>.

13 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, comment 24 (as amended April 10<sup>th</sup>, 2006) [ICSID Convention], March 18<sup>th</sup>, 1965. <http://icsid.worldbank.org/ICSID/ICSID/RulesMain.jsp>.

14 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 (as amended April 10<sup>th</sup>, 2006) [ICSID Convention], March 18<sup>th</sup>, 1965. <http://icsid.worldbank.org/ICSID/ICSID/RulesMain.jsp>.

15 Report of the Executive Directors of the International Bank for Reconstruction and

investor consent as a flexible concept that should be considered in light of the Convention's goals. Consent could viably be understood to include only the elements connected to the investor's specific claim. Equally, it might encompass any violations of international law arising out of the investment underlying the claim. Regardless, there is enough to ambiguity to permit variable interpretations.

*B. Arising out of “the subject matter” and “an investment”*

The second requirement is that the counterclaim arise out of the subject matter of the dispute (art. 46) and arise out of an investment (art. 25).

Article 25.1 states that “*The jurisdiction of the Centre shall extend to any legal dispute arising directly out of an investment between a Contracting State and a national of another Contracting State.*”<sup>16</sup> Additionally, the counterclaim must “*arise directly out of the subject matter of the dispute*” under Article 46.<sup>17</sup>

The questions that tribunals have struggled with are: What legal violations arise out of the investment, what is the subject matter of the dispute, and what may arise directly out of it? The subject matter of the dispute, like consent, may be read narrowly or broadly. If read narrowly, it refers only to counterclaims that are “*indivisible from*” the original investment.<sup>18</sup> If read broadly, the subject matter of the dispute could just refer to the investment at issue and anything connected to it, which would afford more options for State counterclaims. “Arising from an investment” is similarly vague.

The ambiguity of consent, arising from an investment and subject matter of the dispute lends itself to tribunal interpreta-

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Development on the Convention on the Settlement of Investment Disputes between States and Nationals of Other States, comment 24 (as amended April 10<sup>th</sup>, 2006) [ICSID Convention], March 18<sup>th</sup>, 1965. <http://icsid.worldbank.org/ICSID/ICSID/RulesMain.jsp>.

16 Convention on the Settlement of Investment Disputes between States and Nationals of other States, art. 25.1 (as amended April 10<sup>th</sup>, 2006), *ICSID Rules and Regulations* (March 18<sup>th</sup>, 1965). <http://icsid.worldbank.org/ICSID/ICSID/RulesMain.jsp>.

17 Convention on the Settlement of Investment Disputes between States and Nationals of other States, art. 46 (as amended April 10<sup>th</sup>, 2006), *ICSID Rules and Regulations* (March 18<sup>th</sup>, 1965). <http://icsid.worldbank.org/ICSID/ICSID/RulesMain.jsp>.

18 *Saluka Investments BV v. Czech Republic*. Judgment of the Swiss Tribunal, 65, September 7<sup>th</sup>, 2006, Ad hoc-UNCITRAL Rules; IIC 211 (2006).

tion. Outlining cases thus provides a better understanding of the state of current jurisdiction for counterclaims.

#### IV. CASES

International investment dispute tribunals have considered a few State counterclaims over the years. The following section provides an overview of tribunals' decisions thereupon. Surveying these decisions gives a sense of the current status of State claims and counterclaims.

##### *A. Contract-Based Claims*

Early cases arose from breach of investment agreements between the investor and the State (“*contract-based claims*”). These cases generally upheld jurisdiction for counterclaims without discussion. They rejected claims on factual grounds. *Adriano Gardella* (1977),<sup>19</sup> *Southern Pacific Properties* (1985),<sup>20</sup> and *Benvenuti* (1980)<sup>21</sup> reflect this trend. In general, early cases seemed to understand jurisdiction broadly. *Benvenuti*, for example, provides jurisdiction to a counterclaim alleging tax violations and intangible losses.

##### 1. Early Counterclaims *Gardella*

In *Adriano Gardella v. Republic of the Ivory Coast* (1977),<sup>22</sup> Gardella, an Italian company, set up a joint venture hemp factory with the Ivory Coast. The contract provided for ICSID jurisdiction. The investor tried to impose unilateral modifications on the

19 *Adriano Gardella SpA (Claimant) v. Republic of the Ivory Coast*. ICSID Case No. ARB/74/1, Award, August 29<sup>th</sup>, 1977.

20 *Southern Pacific Properties (Middle East) Limited v. Arab Republic of Egypt*. ICSID Case No. ARB/84/3, Decision on Jurisdiction, November 27<sup>th</sup>, 1985.

21 *Benvenuti & Bonfant Company v. the Government of the People's Republic of the Congo*. ICSID Case No. ARB/77/2, Award, August 15<sup>th</sup>, 1980.

22 *Adriano Gardella SpA (Claimant) v. Republic of the Ivory Coast*. ICSID Case No. ARB/74/1, Award, August 29<sup>th</sup>, 1977.

contract, increasing prices and decreasing exports. The government failed to respond. It neither paid the bills nor contested increased prices. Gardella claimed against the government for damages arising from a breach of contract. The government “filed a counterclaim against Gardella for damages arising from Gardella’s termination of the agreement.”<sup>23</sup> Only part of the award was released, so information as to jurisdiction and substance is limited. Indeed, there is not enough information to extract any principles, other than that, “the Tribunal had jurisdiction over the dispute and both the claim and the counterclaim were rejected” on factual grounds.<sup>24</sup>

### *Southern Pacific Properties*

In *Southern Pacific Properties* (1985),<sup>25</sup> Respondent State, Egypt, counterclaimed. All of its counterclaims stemmed directly from the contract that underpinned Southern Pacific’s claim and ICSID jurisdiction.<sup>26</sup> There appears to have been no discussion of jurisdiction. The tribunal off-handedly dismissed the counterclaims: “It results from what the Tribunal has already said that none of these alleged faults was committed and none of them was imputed to the Claimants by the Egyptian authorities as a ground for the cancellation or in any other form before May 28<sup>th</sup>, 1978. It follows that the Counter-Claim is to be dismissed.”<sup>27</sup>

23 *Adriano Gardella SpA (Claimant) v. Republic of the Ivory Coast*. ICSID Case No. ARB/74/1, Award, August 29<sup>th</sup>, 1977.

24 *Adriano Gardella SpA (Claimant) v. Republic of the Ivory Coast*. ICSID Case No. ARB/74/1, Award, August 29<sup>th</sup>, 1977.

25 *Southern Pacific Properties (Middle East) Limited v. Arab Republic of Egypt*. ICSID Case No. ARB/84/3, Decision on Jurisdiction, November 27<sup>th</sup>, 1985.

26 *Southern Pacific Properties (Middle East) Limited v. Arab Republic of Egypt*. ICSID Case No. ARB/84/3, Decision on Jurisdiction, 255, November 27<sup>th</sup>, 1985: “In support of the Counter-Claim, the Respondent invokes certain faults alleged to be attributable to the Claimants, namely: i) the transformation of the project into a housing project; ii) the absence of touristic elements (hotels, commercial centers and villages) in the project; iii) the Claimants’ abandonment of the Ras El Hekma Project; iv) the financial deficiencies of the Claimants; and v) above all, the Claimants’ refusal to cooperate, and particularly to consider the solution of an alternative site.”

27 *Southern Pacific Properties (Middle East) Limited v. Arab Republic of Egypt*. ICSID Case No. ARB/84/3, Decision on Jurisdiction, 256, November 27<sup>th</sup>, 1985.

*Benvenuti*

*Benvenuti v. Congo* (1980)<sup>28</sup> represents a broad reading of “arising from the subject-matter of the dispute.” While the counterclaim failed, it was on factual, not jurisdictional grounds.

*Benvenuti and Bonfant (B&B)*, an Italian company, contracted with the Republic of Congo to set up a company to produce mineral water and make plastic bottles. Later, the parties signed an agreement, creating a mixed company, incorporated in Congo. The Congo held 60% of the company, with the right to purchase B&B's shares in 5 years. In addition, the government guaranteed the company, “plasco,” preferential tax status and to guarantee any requisite financing. Article 12 of the agreement provided recourse to ICSID.<sup>29</sup> Government intervention escalated over the years. Ultimately, most of the Italian staff left after embassy warnings. The Congolese army then occupied the head office. B&B claimed for compensation of shareholdings and non-payment, moral damages, and repayment of loans and advances.

The Government counterclaimed for: “(a) damages for the non-payment of duties and taxes on goods allegedly imported under cover of plasco but intended for third parties; (b) damages for alleged overpricing of raw materials; (c) damages for alleged defaults in the execution of the agreement with sodisca; (d) damages for alleged defects in the construction of the plant; (e) damages for intangible loss (*préjudice moral*), plus interest at 10% per annum.”<sup>30</sup>

In a very short decision, the tribunal both found jurisdiction for the government's counterclaims and dismissed them as unsubstantiated.

*Since the counterclaim related directly to the object of the dispute and came within the competence of the Centre, and since B&B had not challenged the competence of the Tribunal, the Tribunal was obliged by Article 40.1 of the*

28 *Benvenuti & Bonfant Company v. the Government of the People's Republic of the Congo*. ICSID Case No. ARB/77/2, Award, August 15<sup>th</sup>, 1980.

29 *Benvenuti & Bonfant Company v. the Government of the People's Republic of the Congo*. ICSID Case No. ARB/77/2, Award, § 4.103, August 15<sup>th</sup>, 1980.

30 *Benvenuti & Bonfant Company v. the Government of the People's Republic of the Congo*. ICSID Case No. ARB/77/2, Award, § 3.1, August 15<sup>th</sup>, 1980.

*Rules to hold that the counterclaim came within its competence (362-5). The counterclaim was, however, dismissed, on the grounds that the evidence produced by the Government had failed to substantiate any of the heads of the counterclaim.*<sup>31</sup>

It is notable, however, that the tribunal found jurisdiction over all of the government's counterclaims. The counterclaims included “*damages for intangible loss*” and “*damages for non-payment of duties and taxes*.”<sup>32</sup> As will be seen, later tribunals rejected both these grounds as “*not arising from the investment*.”<sup>33</sup> The tribunal here, however, did consider them to arise from an investment –implicitly– and from the subject matter of the dispute –explicitly.

The tribunal then considered the question of whether one or more of the heads of the counterclaim might be beyond its competence, laid down in Article 12 of the Agreement and Article 25 of the Articles of Association. 104. Considering that the counterclaim relates directly to the object of the dispute, that the competence of the Tribunal has not been disputed and that it is within the competence of the Centre.<sup>34</sup>

Likely, the tribunal here understood investment to include actions in furtherance thereof. Thus, taxes, duties and moral damages that “*arose from*” the investment, were fair game. Anything related to the investment or its performance was within the scope of a State counterclaim –including breaches of local law or international law.

This opinion, *albeit in dicta*, provides a good counterexample to later decisions that severely limit the substantive scope of pro-

31 *Benvenuti & Bonfant Company v. the Government of the People's Republic of the Congo*. ICSID Case No. ARB/77/2, Award, § 4.104, August 15<sup>th</sup>, 1980.

32 *Benvenuti & Bonfant Company v. the Government of the People's Republic of the Congo*. ICSID Case No. ARB/77/2, Award, § 4.101, August 15<sup>th</sup>, 1980.

33 See e.g., *Amco Asia Corporation, PanAmerican Development Ltd. and PT Amco Indonesia v. Republic of Indonesia*. Resubmitted Case, ICSID Case No. Arb/81/1, Decision on Jurisdiction, May 10<sup>th</sup>, 1988.

See also, *Saluka Investments BV v. Czech Republic*. Judgment of the Swiss Tribunal, September 7<sup>th</sup>, 2006, Ad hoc-UNCITRAL Rules; IIC 211 (2006).

34 *Benvenuti & Bonfant Company v. the Government of the People's Republic of the Congo*. ICSID Case No. ARB/77/2, Award, §§ 4.103, 4.104, August 15<sup>th</sup>, 1980.

tections for States by introducing a limited reading of “*arising from an investment*” and “*subject matter of the dispute.*”<sup>35</sup>

## 2. Cases Limiting Jurisdiction and Substantive Protections

The *Klöckner v. Cameroon*<sup>36</sup> and *Amco v. Indonesia*<sup>37</sup> decisions were the first to actively consider counterclaim jurisdiction. *Klöckner* upheld jurisdiction where the counterclaim was closely connected to the original claim, but determined that a State could not counterclaim for an equity violation such as misrepresentation.<sup>38</sup> *Amco* rejected jurisdiction. The requirement that the counterclaim “*arise directly from the investment*” excluded violations based solely on domestic law.<sup>39</sup> *RSM v. Grenada*,<sup>40</sup> a recent case, rejected a number of well-supported counterclaims on similar grounds –demonstrating the enduring influence of these two early cases.<sup>41</sup>

### *Klöckner*

*Klöckner* was the first case that analyzed counterclaim jurisdiction. While it finds jurisdiction, later tribunals used its considerations to limit jurisdiction to counterclaims that are “*indivisible from*” the original claim.<sup>42</sup> *Klöckner* is also the first case (in what

35 Convention on the Settlement of Investment Disputes between States and Nationals of other States, art. 25, 46 (as amended April 10<sup>th</sup>, 2006), *ICSID Rules and Regulations* (March 18<sup>th</sup>, 1965). <http://icsid.worldbank.org/ICSID/ICSID/RulesMain.jsp>.

36 *Klöckner Industrie-Anlagen v. United Republic of Cameroon and Société Camerounaise des Engrais*. ICSID Case No. ARB/81/2, Award, October 21<sup>st</sup>, 1983.

37 *Amco Asia Corporation and others v. Republic of Indonesia*. ICSID Case No. ARB/81/1, Award, November 20<sup>th</sup>, 1984.

38 *Klöckner Industrie-Anlagen v. United Republic of Cameroon and Société Camerounaise des Engrais*. ICSID Case No. ARB/81/2, Award, § III, October 21<sup>st</sup>, 1983.

39 *Amco Asia Corporation, PanAmerican Development Ltd. and PT Amco Indonesia v. Republic of Indonesia*. Resubmitted Case, ICSID Case No. Arb/81/1, Decision on Jurisdiction, § E, May 10<sup>th</sup>, 1988.

40 *RSM Production Corporation v. Grenada*. ICSID Case No. ARB/05/14, Award, March 13<sup>th</sup>, 2009.

41 Other recent tribunals, like *Saluka*, *supra* note 18, have also adopted these jurisdictional and substantive limitations.

42 See e.g., *Saluka Investments BV v. Czech Republic*. Judgment of the Swiss Tribunal, 65, September 7<sup>th</sup>, 2006, Ad hoc-UNCITRAL Rules; IIC 211 (2006), quoting *Klöckner Industrie-Anlagen v. United Republic of Cameroon and Société Camerounaise des Engrais*.

becomes pattern) that finds a breach by the investor, but still rejects the counterclaim by limiting the substantive scope of protections to Specifically, *Klöckner* upholds jurisdiction where the framework agreement provided for ICSID jurisdiction and the tribunal located a breach therein. The broad framework agreement trumped a later, more specific, contract's jurisdiction clause. Ultimately, however, the tribunal rejects the counterclaim because States' cannot base a substantive claim on “*misrepresentation*” –as this pushes them into the realm of equity. But, as the annulment committee points out, the original tribunal did *de facto* honor the counterclaim when it refused to award certain damages to the investor.

Klöckner, a German company, brought a claim against Cameroon under ICSID. Klöckner and Cameroon had entered into a joint-venture agreement, to supply, erect, and manage a fertilizer company for 5 years minimum. The framework agreement provided for ICSID jurisdiction. A later contract, governing Klöckner's management duties, gave the ICC jurisdiction. Klöckner bought a claim against Cameroon after Cameroon shut down the factory in 1980. Lack of profitability motivated the closure. Cameroon counterclaimed, alleging misrepresentation by Klöckner about its management capabilities, which, among other things, rendered the company unprofitable.<sup>43</sup>

The 1983 award –sustained by the annulment committee– upheld jurisdiction for the counterclaim. The tribunal reasoned that investor consent in one contract applies to any duties housed within that contract.<sup>44</sup> This remained true even though a later contract that explicitly covered those duties provided for jurisdiction in another forum (the ICC).<sup>45</sup> The tribunal gave preference to the first, broad contract (framework agreement) for matters

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ICSID Case No. ARB/81/2, Award, § III, October 21<sup>st</sup>, 1983.

43 *Klöckner Industrie-Anlagen v. United Republic of Cameroon and Société Camerounaise des Engrais*. ICSID Case No. ARB/81/2, Award, § I, October 21<sup>st</sup>, 1983.

44 *Klöckner Industrie-Anlagen v. United Republic of Cameroon and Société Camerounaise des Engrais*. ICSID Case No. ARB/81/2, Award § III, October 21<sup>st</sup>, 1983.

45 *Klöckner Industrie-Anlagen v. United Republic of Cameroon and Société Camerounaise des Engrais*. ICSID Case No. ARB/81/2, Award, § III, October 21<sup>st</sup>, 1983.

that did not exclusively arise out of the second, narrow contract (management agreement).<sup>46</sup> In justifying its decision, the tribunal made a few comments that later tribunals adopt as jurisdictional limitations. Specifically, that the counterclaim based on the framework agreement and the primary claim asserted by the Claimant were “*an indivisible whole*,”<sup>47</sup> that they shared “*a common origin, identical sources, and an operational unity*,”<sup>48</sup> and that both sought “*the accomplishment of a single goal*.”<sup>49</sup>

The annulment committee somewhat reluctantly upheld jurisdiction. After determining that it was possible to locate the breach in the first contract, the annulment committee found that the tribunal did not manifestly exceed its powers.<sup>50</sup> In support, the annulment committee determined that the first contract was a framework agreement. Citing *Holiday Inns*, the tribunal found that “*there is consequently a single legal relationship, even if three cosuccessive legal instruments were concluded. This is so because the first, the Protocol Agreement, encompasses and contains all three*.”<sup>51</sup>

Although both tribunals found that they had jurisdiction to hear the counterclaim, ultimately, they rejected the counterclaim. The annulment committee explains and upholds the original tribunal's rejection of the counterclaim.

*[T]he Award denies that the Cameroonian State could be entitled to claim compensation for ‘the fact that it was misled by a private company’; whether it was deceived or not changes nothing: it acted with either full understanding or with open eye, and if it was ‘misled’, it would have a ‘concurrent responsibility’ which excludes the counterclaim. Therefore, we also seem*

46 *Klöckner Industrie-Anlagen v. United Republic of Cameroon and Société Camerounaise des Engrais*. ICSID Case No. ARB/81/2, Award, §§ III, VI(E), October 21<sup>st</sup>, 1983.

47 *Klöckner Industrie-Anlagen v. United Republic of Cameroon and Société Camerounaise des Engrais*. ICSID Case No. ARB/81/2, Award, § III, October 21<sup>st</sup>, 1983.

48 *Klöckner Industrie-Anlagen v. United Republic of Cameroon and Société Camerounaise des Engrais*. ICSID Case No. ARB/81/2, Award, § VI(C), October 21<sup>st</sup>, 1983.

49 *Klöckner Industrie-Anlagen v. United Republic of Cameroon and Société Camerounaise des Engrais*. ICSID Case No. ARB/81/2, Award, § VI(C), October 21<sup>st</sup>, 1983.

50 *Klöckner v. Cameroon*. ICSID Case No. ARB/81/2, Decision on Application for Annulment, 52, May 3<sup>rd</sup>, 1985.

51 *Klöckner v. Cameroon*. ICSID Case No. ARB/81/2, Decision on Application for Annulment, 24(c), May 3<sup>rd</sup>, 1985.

*to find ourselves here in the field of 'equity', relying on the notions of 'preclusions' or 'estoppel'.<sup>52</sup>*

Later, however, the committee sustained Claimant's objection regarding an inconsistency in the tribunal's reasoning.

*In addition to failure to state reasons, this curious determination of the amount of Klöckner's indemnification amounts to a contradiction in reasons, since the Tribunal assigns responsibility for operating losses to Klöckner and thus accepts the counterclaim, which it expressly rejected on the grounds that operating losses could not be charged to Klöckner. The same is true for the repair costs which were required for the factory to resume operation...<sup>53</sup>*

The original tribunal thus rejected the counterclaim, but took it into account when determining culpability and damages—predicting a modern trend. Interestingly, recent decisions, like *Plama*, find illegality in exactly these situations and thus refuse jurisdiction.<sup>54</sup> Perhaps explained by decisions like *Klöckner*, State counterclaims are not understood to include violations of such principles.

#### *Amco v. Indonesia*

The *Klöckner* tribunal excludes equity from the substantive scope of State counterclaims. *Amco* goes further and excludes violations of law related to the investment. Both *Amco* tribunals read “*arising from an investment*” narrowly, setting a precedent followed by later tribunals.

*Amco v. Indonesia* is also important because it deals with both counterclaims within the original claim and later counterclaims introduced by the State in a resubmitted award. Subsequent State claims raised additional questions of jurisdiction under ICSID Articles 55 and 53.

52 *Klöckner v. Cameroon*. ICSID Case No. ARB/81/2, Decision on Application for Annulment, 123, May 3<sup>rd</sup>, 1985.

53 *Klöckner v. Cameroon*. ICSID Case No. ARB/81/2, Decision on Application for Annulment, 172, May 3<sup>rd</sup>, 1985.

54 *Plama Consortium Limited v. Republic of Bulgaria*. ICSID Case No. ARB/03/24, Decision on Jurisdiction, February 8<sup>th</sup>, 2005.

An American Corporation, Amco, and PT Wisma, an Indonesian company, entered into a Lease and Management Agreement. The Indonesian government directed the process. Amco agreed to invest in and manage a hotel and office complex for 30 years. PT Wisma and Amco fought. PT Wisma forcibly took over the hotel. Indonesia then revoked Amco's business license.<sup>55</sup>

The Lease and Management Agreement provided recourse to ICSID arbitration.<sup>56</sup> Amco initiated ICSID arbitration alleging damages from the termination of the license and loss of the hotel.

The original tribunal applied international law and Indonesian law.<sup>57</sup> The tribunal ruled for *Amco Case*, finding that Indonesia breached international law –inadequate protections for aliens with respect to the takeover and due process violations for the license revocation.<sup>58</sup> The *ad hoc* committee then annulled the award for failure to state reasons. Amco resubmitted the dispute –making similar claims.<sup>59</sup> The resubmission tribunal again found that Indonesia's actions violated international law.<sup>60</sup>

Indonesia counterclaimed in both arbitrations, raising similar issues. In the first proceedings, “*Respondent presented*

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55 *Amco Asia Corporation and others v. Republic of Indonesia*. ICSID Case No. ARB/81/1, Award, November 20<sup>th</sup>, 1984.

56 *Amco Asia Corporation and others v. Republic of Indonesia*. ICSID Case No. ARB/81/1, Award, November 20<sup>th</sup>, 1984. Article IX of the said Application provides as follows: “*If at a later date there is a disagreement and dispute between the business and the government, this disagreement will be put before the International Centre for Settlement of Investment Disputes, in which body the Government of the Republic of Indonesia and the United States are members. All the decisions made by the Convention mentioned above will bind the sides which are in disagreement and dispute.*”

57 *Amco Asia Corporation and others v. Republic of Indonesia*. ICSID Case No. ARB/81/1, Award, 148, November 20<sup>th</sup>, 1984. “*The parties having not expressed an agreement as to the rules of law according to which the disputes between them should be decided, the Tribunal has to apply Indonesian law, which is the law of the Contracting State Party to the dispute, and such rules of international law as the Tribunal deems to be applicable, considering the matters and issues in dispute.*”

58 *Amco Asia Corporation and others v. Republic of Indonesia*. ICSID Case No. ARB/81/1, Award, November 20<sup>th</sup>, 1984.

59 *Amco Asia Corporation, PanAmerican Development Ltd. and PT Amco Indonesia v. Republic of Indonesia*. ICSID Case No. ARB/81/1, Decision on the Application for Annulment, May 16<sup>th</sup>, 1986.

60 *Amco Asia Corporation, PanAmerican Development Ltd. and PT Amco Indonesia v. Republic of Indonesia*. Resubmitted Case, ICSID Case No. Arb/81/1, Decision on Jurisdiction, May 10<sup>th</sup>, 1988.

*a counterclaim seeking the payment by Claimants of all monies they should have paid as taxes and import duties, but for the tax holiday granted by the licence.*<sup>61</sup> The “missing” taxes resulted from the tax breaks afforded to Amco by their business license, which no longer applied once the license was revoked. The tribunal refused to honor Indonesia's claim because they found the revocation illegal.<sup>62</sup>

The *ad hoc* committee annulled the prior tribunal's finding that the license was unlawful. As a result “*the part of the Award dismissing the counterclaim for recovery of the tax and import facilities has to be annulled as well.*”<sup>63</sup>

Before the resubmission tribunal, Indonesia claimed that Amco engaged in tax fraud through “*a systemic course of tax evasion ... over many years.*”<sup>64</sup> The tribunal considered the following:

*In the view of the Tribunal the issue falls to be decided in relation to three questions. First, is the claim of tax fraud a new claim or an old claim, in the sense that it had or had not been advanced before the First Tribunal? Second, if it is a new claim, are new claims in principle admissible before a new Tribunal established by request of the parties subsequent to annulment or partial annulment of the Award of the First Tribunal? And third, if the answer to the second question is in the affirmative, is this particular claim within the jurisdiction of the present Tribunal ratione materiae?*<sup>65</sup>

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61 *Amco Asia Corporation and others v. Republic of Indonesia*. ICSID Case No. ARB/81/1, Award, 283, November 20<sup>th</sup>, 1984.

62 *Amco Asia Corporation and others v. Republic of Indonesia*. ICSID Case No. ARB/81/1, Award, 287, November 20<sup>th</sup>, 1984. “*This being said, the Tribunal notes that in the instant case, the revocation of the tax facilities which were attached to the licence, was decided in the BKPM [Badan Koordinasi Penanaman Modal] Chairman's decision of July 9, 1980 (see above, paras. 128-130) as a result of the revocation of the licence. Accordingly, since the Tribunal finds that the revocation of the licence was unlawful, as a consequence, the revocation of the tax facilities was unlawful as well.*”

63 *Amco Asia Corporation, PanAmerican Development Ltd. and PT Amco Indonesia v. Republic of Indonesia*. ICSID Case No. ARB/81/1, Decision on the Application for Annulment, 116, May 16<sup>th</sup>, 1986.

64 *Amco Asia Corporation, PanAmerican Development Ltd. and PT Amco Indonesia v. Republic of Indonesia*. Resubmitted Case, ICSID Case No. Arb/81/1, Decision on Jurisdiction, May 10<sup>th</sup>, 1988.

65 *Amco Asia Corporation, PanAmerican Development Ltd. and PT Amco Indonesia v. Republic of Indonesia*. Resubmitted Case, ICSID Case No. Arb/81/1, Decision on Jurisdiction, § E, May 10<sup>th</sup>, 1988.

With regard to the first issue, new or old claim, the tribunal took a formalistic approach. The tribunal found that although Indonesia raised tax fraud before the first tribunal, it was not raised in the form of a claim or counterclaim. Therefore it was a new counterclaim and must be considered as such. “*The fact that argument was exchanged (...) does not mean that tax fraud was a claim in existence before the first Tribunal. For that to have been so, it would have been necessary for it to have been advanced as a counterclaim or as an additional claim under Rule 40.*”<sup>66</sup> Since the counterclaim did not meet the procedural requirement, the tribunal considered it a new counterclaim. The tribunal thus considered jurisdiction *de novo*.<sup>67</sup>

The tribunal then considered “*Amco's contention that tax fraud is outside the jurisdiction of the present Tribunal ratione materiae.*”<sup>68</sup> The tribunal agreed with Amco, finding that a claim for tax fraud is not “*a legal dispute arising directly out of an investment,*” as required under Article 25.1.<sup>69</sup>

In finding this, the tribunal first accepts that some tax claims would be considered “*a legal dispute arising out of an investment.*”<sup>70</sup> The tribunal finds that this particular claim is not one of those. The tribunal creates the following distinction:

*In answering this question the Tribunal believes that it 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*

66 *Amco Asia Corporation, PanAmerican Development Ltd. and PT Amco Indonesia v. Republic of Indonesia*. Resubmitted Case, ICSID Case No. Arb/81/1, Decision on Jurisdiction, § E(1), May 10<sup>th</sup>, 1988.

67 *Amco Asia Corporation, PanAmerican Development Ltd. and PT Amco Indonesia v. Republic of Indonesia*. Resubmitted Case, ICSID Case No. Arb/81/1, Decision on Jurisdiction, § E(1), May 10<sup>th</sup>, 1988.

68 *Amco Asia Corporation, PanAmerican Development Ltd. and PT Amco Indonesia v. Republic of Indonesia*. Resubmitted Case, ICSID Case No. Arb/81/1, Decision on Jurisdiction, § E (2), May 10<sup>th</sup>, 1988.

69 *Amco Asia Corporation, PanAmerican Development Ltd. and PT Amco Indonesia v. Republic of Indonesia*. Resubmitted Case, ICSID Case No. Arb/81/1, Decision on Jurisdiction, § E (2), May 10<sup>th</sup>, 1988.

70 *Amco Asia Corporation, PanAmerican Development Ltd. and PT Amco Indonesia v. Republic of Indonesia*. Resubmitted Case, ICSID Case No. Arb/81/1, Decision on Jurisdiction, § E (2), May 10<sup>th</sup>, 1988: “*In fact, both parties agree, as does the Tribunal, that tax claims may be within ICSID's jurisdiction and that claims in relation thereto would be available to both parties to an investment dispute.*”

*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 fall to be decided by the appropriate procedures in the relevant jurisdiction unless the general law generates an investment dispute under the Convention.*<sup>71</sup>

According to the tribunal, “*The obligation not to engage in tax fraud is clearly a general obligation of law in Indonesia. It was not specially contracted for in the investment agreement and does not arise directly out of the investment.*”<sup>72</sup> This reading, which later tribunals follow, represents a significant limitation on substantive legal protections for States under ICSID.

With respect to new claims in a resubmitted case, the tribunal endorsed a much more restrictive reading than that espoused by expert, Aron Broches. Broches argued that “*there is no justification for arbitrarily reading into the Convention a restriction on a party's right to present claims or counterclaims other than the dispositive one of Arbitration Rule 55.3.*”<sup>73</sup> In support, Broches quoted Article 46, which he understood to impose few limitations.<sup>74</sup>

The tribunal agreed that Article 46 contains few limitations on counterclaims. According to the tribunal, however, Article 40 imposes procedural limits on Article 46 for original cases.<sup>75</sup> Additionally, 52.6 and 55.3 govern resubmitted disputes and

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71 *Amco Asia Corporation, PanAmerican Development Ltd. and PT Amco Indonesia v. Republic of Indonesia*. Resubmitted Case, ICSID Case No. Arb/81/1, Decision on Jurisdiction, § E (2), May 10<sup>th</sup>, 1988.

72 *Amco Asia Corporation, PanAmerican Development Ltd. and PT Amco Indonesia v. Republic of Indonesia*. Resubmitted Case, ICSID Case No. Arb/81/1, Decision on Jurisdiction, § E (2), May 10<sup>th</sup>, 1988.

73 *Amco Asia Corporation, PanAmerican Development Ltd. and PT Amco Indonesia v. Republic of Indonesia*. Resubmitted Case, ICSID Case No. Arb/81/1, Decision on Jurisdiction, § E(3), May 10<sup>th</sup>, 1988.

74 *Amco Asia Corporation, PanAmerican Development Ltd. and PT Amco Indonesia v. Republic of Indonesia*. Resubmitted Case, ICSID Case No. Arb/81/1, Decision on Jurisdiction, § E(3), May 10<sup>th</sup>, 1988.

75 *Amco Asia Corporation, PanAmerican Development Ltd. and PT Amco Indonesia v. Republic of Indonesia*. Resubmitted Case, ICSID Case No. Arb/81/1, Decision on Jurisdiction, § E(3), May 10<sup>th</sup>, 1988: “*But Article 46 is to be read together with Rule 40, which provides specific procedures and time limits...*” Thus, the tribunal imposes temporal and procedural limits on counterclaims, but not substantive or jurisdictional limitations.

impose heightened limitations on counterclaims.<sup>76</sup> “Article 52 is not a provision for starting a totally new arbitration, restricted only by the requirements of Article 25. Rather, it is a procedure for resubmission of an existing dispute in respect of which Article 25 jurisdiction exists.”<sup>77</sup> The tribunal reads “existing dispute” to include only the causes of action in the original claim.<sup>78</sup> The claim for tax fraud was not a cause of action in the original claim, so it was excluded.

A number of relevant points may be extracted from this decision. First, a State that considers counterclaiming should raise the claim in the proper format (under Rule 40) as soon as possible. Second, under *Amco*, a State will struggle to bring a counterclaim in a resubmitted case that it did not already raise as a counterclaim. Third, a State should understand that where a tribunal applies *Amco's* vision of substantive legal protections, the State is not on equal footing with an investor. While an investor may point to violations of non-contract domestic law as violations of an investment agreement, a State may not –even where the applicable law is domestic law. Tax fraud was not considered “*arising from the investment*” under Article 25, even though the tax fraud was potentially based on money owed as a result of or in performing the investment.

76 *Amco Asia Corporation, PanAmerican Development Ltd. and PT Amco Indonesia v. Republic of Indonesia*. Resubmitted Case, ICSID Case No. Arb/81/1, Decision on Jurisdiction, § E(3), May 10<sup>th</sup>, 1988.

77 *Amco Asia Corporation, PanAmerican Development Ltd. and PT Amco Indonesia v. Republic of Indonesia*. Resubmitted Case, ICSID Case No. Arb/81/1, Decision on Jurisdiction, § E(3), May 10<sup>th</sup>, 1988. This statement is supported by the following: “Nor is the matter resolved by reference to Article 25, for while indeed the jurisdiction of the Centre shall extend to ‘any legal dispute arising out of an investment’ Article 52.6 (which presupposes that Article 25 jurisdiction already exists) states that if an award is annulled ‘the dispute’ shall be submitted to a new Tribunal.”

78 *Amco Asia Corporation, PanAmerican Development Ltd. and PT Amco Indonesia v. Republic of Indonesia*. Resubmitted Case, ICSID Case No. Arb/81/1, Decision on Jurisdiction, § E(3), May 10<sup>th</sup>, 1988. According to the tribunal, “the wording of Rule 55(3), which covers this situation, signifies that this is not a totally new proceeding constrained only by Article 25 (and by consideration of *res judicata*). It is a reconsideration of the dispute.” The tribunal then goes on to define the dispute in a very limited manner. It looks to Note B to Rule 55, which states in relevant part “A dispute is defined by claims formally asserted and responded to in claim and defence, or in counterclaim and reply to counterclaim –in other words, the causes of action.” “The dispute or ‘the former’ dispute is necessarily the dispute as formulated in the pleadings before the First Tribunal whose Award (save insofar as it is *res judicata*) is now being reconsidered.”

*RSM Production Corporation v. Grenada*

RSM, an American company, brought a claim pursuant to an ICSID arbitration clause in an agreement between RSM and Grenada.<sup>79</sup> Grenada's laws (English law) were the applicable laws under the agreement.<sup>80</sup> The contract provided RSM with the option to acquire rights to explore and potentially extract offshore oil and gas reserves, if RSM applied within 90 days.

Both parties knew that the reserves were in disputed waters. Trinidad & Tobago, Grenada, and Venezuela all claimed the area. As a result, the agreement had a broad *force majeure* clause. It obligated RSM to “take all reasonable steps to remove the cause” of the *force majeure*.<sup>81</sup> Two weeks after the agreement, RSM invoked the *force majeure* clause, pausing the 90-day application period for the next 8 years.

During those 8 years, Mr. Jack Grynberg, the owner of RMS, tried to strong-arm Venezuela and Trinidad & Tobago into ceding the contested waters to Grenada. Mr. Grynberg's tactics included: threatening Trinidad with ICSID arbitration and then threatening Grenada with arbitration when it refused to join; threatening Venezuela; and writing letters with clear falsehoods.<sup>82</sup> All this was done over Grenada's vocal objections.

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79 *RSM Production Corporation v. Grenada*. ICSID Case No. ARB/05/14, Award, March 13<sup>th</sup>, 2009. The agreement stated that “Article 26. Any dispute or difference arising between the parties relating to the construction, meaning or effect of this Agreement or the rights or liabilities of the parties hereunder, or any matter arising out of the same or connected therewith shall be resolved amicably by negotiations. ... (a) Any unresolved dispute or difference aforesaid shall be submitted for settlement by arbitration to the International Centre for the Settlement of Investment Disputes (ICSID) established by the Convention for the Settlement of Investment Disputes between States and Nationals of other States of 16 March 1965 and for this purpose it is agreed that although the Company (as an investor) is a company.”

80 *RSM Production Corporation v. Grenada*. ICSID Case No. ARB/05/14, Award, 12, March 13<sup>th</sup>, 2009.

81 *RSM Production Corporation v. Grenada*. ICSID Case No. ARB/05/14, Award, 61, March 13<sup>th</sup>, 2009.

82 *RSM Production Corporation v. Grenada*. ICSID Case No. ARB/05/14, Award, 326, March 13<sup>th</sup>, 2009: “Under Article 24.2 RSM was obliged to take all reasonable steps to remove the cause of the *force majeure* – to assist in resolving the maritime boundaries. Instead, RSM's actions substantially hindered such resolution. RSM authorised false maps that purportedly favoured Trinidad & Tobago as part of this negotiating process; and RSM then suggested that the Agreement Area be enlarged deliberately to provoke Trinidad & Tobago, a friendly neighbouring State. Mr. Grynberg aggressively pursued unilateral legal proceedings before ICSID and ITLOS [International Tribunal for the Law of the Sea], even threatening Grenada

8 years later, RSM revoked *force majeure* and applied for the exploration license. However, the tribunal found that more than the allotted 90 days passed between revoking *force majeure* and applying for the license. The tribunal thus denied RSM's claims.<sup>83</sup>

Grenada counterclaimed under three heads: (1) RSM fraudulently induced Grenada to enter the contract through material misrepresentations;<sup>84</sup> (2) RSM failed to take all reasonable efforts to remove the cause of *force majeure* and in fact hindered it; and (3) RSM damaged local fisherman when engaging in unauthorized research, and thus owed EC\$391,860.00 to cover Grenada's expenses in compensating the damaged fishermen.

The tribunal found that RSM did misrepresent several important facts that Grenada relied when deciding to enter into the Agreement. Still, the tribunal rejected the counterclaim. Where misrepresentations occurred, the tribunal found that Mr. Grynberg believed what he said. Therefore they were not fraudulent misrepresentations. According to the tribunal, under applicable law only fraudulent misrepresentations are compensable.

The tribunal also rejected Grenada's counterclaim for damages to local fisherman in breach of the contract and local criminal law. The tribunal "*does not accept Grenada's submission that, implicitly, RSM bore a like contractual obligation to that imposed*

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*in the process if it would not join him in this strategy. Then RSM wrote a threatening letter directly to the Prime Minister of Trinidad & Tobago, riddled with misleading statements, which was widely disseminated by RSM to foreign diplomatic and government officials causing significant embarrassment to Grenada. In addition to the traditionally friendly relations between Grenada and Trinidad & Tobago, it is necessary to recall that after Grenada had suffered severe hurricane-damage only a few years previously, its large neighbour had generously assisted Grenada's population with emergency and other substantial aid."*

83 *RSM Production Corporation v. Grenada*. ICSID Case No. ARB/05/14, Award, 377, March 13<sup>th</sup>, 2009.

84 *RSM Production Corporation v. Grenada*. ICSID Case No. ARB/05/14, Award, 400, March 13<sup>th</sup>, 2009: "(a) that RSM had sufficient financial resources to fulfill its intended obligations under the Agreement; (b) that RSM intended to commence work under the Agreement immediately after its entry into force, (c) that RSM by itself would perform its Agreement obligations rather than 'farm out' all financial risks and contractual commitments to other entities; and (d) that Mr Grynberg had expertise as a negotiator in maritime boundary delimitations."

See also *id.*, at 99: "RSM deliberately violated Grenadian statutory law and international law in February 2004, when RSM caused a vessel to enter Grenadian waters and conduct seismic research without permission. Such action violated Article 4 of the 1989 Act; and it also breached the Agreement."

by statute under Grenada's criminal law. Such a broad implied term in the Agreement has no legal basis under Grenadian law.”<sup>85</sup>

This represents one of the first opportunities a tribunal had to determine the impact of damages resulting from harm to the local population. They chose to read “*arising out of the subject-matter of the dispute*” and “*arising out of an investment*” narrowly to exclude criminal violations that related to the investment. That said, there appears to be no reason that a tribunal could not require an investor to act in accordance with domestic law, particularly where the crime was done in furtherance of the investment at issue. Tribunals like *CSOB*, for example, read “*arising from an investment*” broadly.

*An investment is frequently a rather complex operation, composed of various interrelated transactions, each element of which, standing alone, might not in all cases qualify as an investment. Hence, a dispute that is brought before the Centre must be deemed to arise directly out of an investment even when it is based on a transaction which, standing alone, would not qualify as an investment under the Convention, provided that the particular transaction forms an integral part of an overall operation that qualifies as an investment.*<sup>86</sup>

The tribunal then denied Grenada's *force majeure* claim for lack of causation. It found that “*RSM's secretive, unilateral, unauthorized, crude ‘horse-trading’ approach, backed up with wild threats and vexatious litigation if unsuccessful, contradicted the essential principles of maritime boundary negotiations between States.*”<sup>87</sup> In light of the evidence, “*the Tribunal concludes that Mr. Grynberg's actions in relation to the Grenada-Venezuela maritime boundary negotiations constituted a breach of RSM's obligations under Article 24.2 of the Agreement.*”<sup>88</sup> The tribunal refused the

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85 *RSM Production Corporation v. Grenada*. ICSID Case No. ARB/05/14, Award, 471, March 13<sup>th</sup>, 2009.

86 *RSM Production Corporation v. Grenada*. ICSID Case No. ARB/05/14, Award, ft. 29, March 13<sup>th</sup>, 2009.

87 *RSM Production Corporation v. Grenada*. ICSID Case No. ARB/05/14, Award, 327, March 13<sup>th</sup>, 2009.

88 *RSM Production Corporation v. Grenada*. ICSID Case No. ARB/05/14, Award, 307, March 13<sup>th</sup>, 2009: “*In light of all this evidence, the Tribunal concludes that Mr Grynberg's actions on behalf of RSM in relation to the Grenada-Trinidad & Tobago maritime boundary*

claim, however, for lack of causation. “*The question remains what effect was caused by RSM’s contractual breach. On the evidence adduced before the Tribunal, it cannot be said to have deprived the Respondent of substantially the whole benefit of the Agreement.*”<sup>89</sup> Continuing, “*Thus, whilst there was certainly embarrassment and diplomatic difficulties for Grenada, no cogent evidence was adduced of any injury to Grenada measurable in money damages to compensate it for RSM’s contractual breach.*”<sup>90</sup>

In the end, raising counterclaims may have hurt Grenada. The tribunal decided to split costs because both the investor and the State had been unsuccessful in their claims.<sup>91</sup> Discouragement of counterclaims might seem rather odd—considering their systemic importance and lack of success.

### 3. Cases Reducing Awards

Not all counterclaims were for naught. The *Klöckner* tribunal is certainly not the only tribunal to reject counterclaims while factoring them into damages. Indeed, some might say the *Klöckner* tribunal predicted a trend. *Atlantic Triton*,<sup>92</sup> *MINE*,<sup>93</sup> and *Desert Line*<sup>94</sup> are three such cases.

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*negotiations also breached RSM’s obligation under Article 24.2 of the Agreement”.*

89 *RSM Production Corporation v. Grenada*. ICSID Case No. ARB/05/14, Award, 309, March 13<sup>th</sup>, 2009.

90 *RSM Production Corporation v. Grenada*. ICSID Case No. ARB/05/14, Award, 309, March 13<sup>th</sup>, 2009: This opinion is reflected throughout the award: “*As a result, the actions of RSM, although amounting to breaches of Article 24.2 cannot be said to have deprived the Respondent of substantially the whole benefit of the Agreement. As was the case with Venezuela, if Grenada and Trinidad and Tobago had been ready to resolve their maritime boundaries, they could have done so in spite of Mr. Grynberg’s behaviour. Nor did RSM cause Grenada any loss measurable in money damages to compensate for its contractual breach under the law of Grenada*”.

91 *RSM Production Corporation v. Grenada*. ICSID Case No. ARB/05/14, Award, 495-496, March 13<sup>th</sup>, 2009.

92 *Atlantic Triton Company Limited v. People’s Revolutionary Republic of Guinea*. ICSID Case No. ARB/84/1, Award, April 21<sup>st</sup>, 1986.

93 *Maritime International Nominees Establishment (MINE) v. Republic of Guinea*. ICSID Case No. ARB/84/4, Award, January 6<sup>th</sup>, 1988.

94 *Desert Line Projects LLC v. Republic of Yemen*. ICSID Case No. ARB/05/17 (Oman- Republic of Yemen BIT), Award, February 6<sup>th</sup>, 2008.

*Atlantic Triton (1986)*

Atlantic Triton commenced ICSID arbitration proceedings against Guinea in 1984. Atlantic Triton requested repayment of money owed; payment of management costs; indemnification for damages; and moral damages after a failed joint venture with Guinea. Guinea counterclaimed for “*damages and interest for breach of Atlantic Triton's contractual undertakings in respect of the seizures, the costs of restoration and refit of the vessels and the mechanical breakdowns of the vessels.*”<sup>95</sup>

The tribunal appears to assume jurisdiction for the counterclaim without discussion. This is likely because the counterclaim is directly based on the contract underpinning Atlantic's claim. The tribunal rejected the counterclaim on factual grounds. “*While it was clear that the undertaking as a whole had been a failure, Guinea had not succeeded in showing that this failure resulted from poor management by Atlantic Triton as opposed to lack of financial and material means and from insufficient initial investment in equipment and infrastructures.*”<sup>96</sup>

Interestingly, while the tribunal rejected the counterclaim, mirroring the Klöckner tribunal, it took the counterclaim into account when considering damages. “*Atlantic Triton's contractual undertakings in respect of the seizures [are a] consideration in reducing the amount of outstanding management fees awarded to it.*”<sup>97</sup> Thus while “*Guinea was responsible for many of the shortcomings itself,*” and so there “*was no ground for awarding Guinea damages for losses,*”<sup>98</sup> the tribunal reduced damages in response to the counterclaim.<sup>99</sup> The Klöckner annulment tribunal might argue that this was a successful counterclaim.

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95 *Atlantic Triton Company Limited v. People's Revolutionary Republic of Guinea*. ICSID Case No. ARB/84/1, Award, April 21<sup>st</sup>, 1986.

96 *Atlantic Triton Company Limited v. People's Revolutionary Republic of Guinea*. ICSID Case No. ARB/84/1, Award, § 8, April 21<sup>st</sup>, 1986.

97 *Atlantic Triton Company Limited v. People's Revolutionary Republic of Guinea*. ICSID Case No. ARB/84/1, Award, § IV(2), April 21<sup>st</sup>, 1986.

98 *Atlantic Triton Company Limited v. People's Revolutionary Republic of Guinea*. ICSID Case No. ARB/84/1, Award, § 8, April 21<sup>st</sup>, 1986.

99 *Atlantic Triton Company Limited v. People's Revolutionary Republic of Guinea*. ICSID

*MINE v. Republic of Guinea*

This case may be the only truly successful counterclaim. Here, Guinea counterclaimed against MINE for legal costs arising from two earlier lawsuits that MINE brought in inappropriate forums. The tribunal awards Guinea some of those legal costs.

*“Guinea makes two counterclaims for damages resulting from MINE’s disregard of the parties’ agreement to arbitrate disputes under the Convention before ICSID.”*<sup>100</sup> First, *“Guinea claims reimbursement of \$322,090.90 in legal fees and expenses that it incurred in order to reverse the United States District Court’s confirmation of the AAA award.”*<sup>101</sup> Second, *“Guinea counterclaims for \$311,309.87 in legal expenses that it incurred in order to obtain the release of the attachments which resulted from MINE’s non-compliance with the Tribunal’s recommendation.”*<sup>102</sup> Specifically, *“[i]n the eighteen months that followed MINE’s first attachment, one Belgian court and three Swiss courts acknowledged the exclusivity of ICSID’s jurisdiction in this dispute. MINE’s pursuit of remedies outside the ICSID proceeding is said to have caused Guinea great embarrassment and extraordinary legal expenses, for which it should be reimbursed.”*<sup>103</sup>

The tribunal found that because Guinea failed to make a timely objection to AAA (American Arbitration Association) jurisdiction, the counterclaim for legal fees and expenses paid to the US Court failed.<sup>104</sup> With respect to remedies sought in Belgian and Swiss Courts, *“the Tribunal considers that MINE’s actions in those nations were contrary to the exclusive jurisdiction*

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Case No. ARB/84/1, Award, *Id.* § 4.1, April 21<sup>st</sup>, 1986.

100 *Maritime International Nominees Establishment (MINE) v. Republic of Guinea*. ICSID Case No. ARB/84/4, Award, § 10(A), January 6<sup>th</sup>, 1988.

101 *Maritime International Nominees Establishment (MINE) v. Republic of Guinea*. ICSID Case No. ARB/84/4, Award, § 10(A), January 6<sup>th</sup>, 1988.

102 *Maritime International Nominees Establishment (MINE) v. Republic of Guinea*. ICSID Case No. ARB/84/4, Award, § 10(A), January 6<sup>th</sup>, 1988.

103 *Maritime International Nominees Establishment (MINE) v. Republic of Guinea*. ICSID Case No. ARB/84/4, Award, § 10(b), January 6<sup>th</sup>, 1988.

104 *Maritime International Nominees Establishment (MINE) v. Republic of Guinea*. ICSID Case No. ARB/84/4, Award, § 10(a), January 6<sup>th</sup>, 1988.

*granted ICSID in this proceeding.*<sup>105</sup> Accordingly, “*Upon consideration of the arguments on this counterclaim, the Tribunal awards Guinea the sum of \$210,000 toward its costs and legal fees relating to the attachment proceedings in Belgium and Switzerland.*”<sup>106</sup>

### *Desert Line*

*In a recent case, Desert Line (2008), Claimant brought a claim against Yemen under the Yemen-Oman BIT. Yemen counterclaimed.*<sup>107</sup> *The tribunal dismissed the counterclaims.*<sup>108</sup> *The Tribunal, however, reduced the award by the amount of one of the counterclaims.*<sup>109</sup> The award does not enter into a discussion of jurisdiction. It merely dismissed the claims on the facts.

This reflects a pattern. Claims are either dismissed on their merits or are dismissed on jurisdictional grounds where they have merit.

### *B. State Counterclaims Under an IIA*

State counterclaims stemming from investment contracts provide space for a more liberal interpretation of consent and arising from the subject matter and investment. BITs, as explored below,

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105 *Maritime International Nominees Establishment (MINE) v. Republic of Guinea*. ICSID Case No. ARB/84/4, Award, § 10(b), January 6<sup>th</sup>, 1988

106 *Maritime International Nominees Establishment (MINE) v. Republic of Guinea*. ICSID Case No. ARB/84/4, Award, § 10(b), January 6<sup>th</sup>, 1988. This will certainly be easier with respect to a contract signed between an investor and a state. As interpreted, IIAs do not tend to limit use of alternative forums until after the ICSID claim.

107 *Desert Line Projects LLC v. Republic of Yemen*. ICSID Case No. ARB/05/17 (Oman-Republic of Yemen BIT), Award, February 6<sup>th</sup>, 2008. “*Yemen is entitled to damages by way of counterclaim resulting from (i) DLP's breach of its undertakings subscribed to in the Settlement Agreement; and (ii) damages and/or set off for DLP's unfulfilled construction obligations and its obligation to maintain the bank guarantees.*”

108 *Desert Line Projects LLC v. Republic of Yemen*. ICSID Case No. ARB/05/17 (Oman-Republic of Yemen BIT), Award, February 6<sup>th</sup>, 2008. “*The Respondent's counterclaims should be dismissed.*”

109 *Desert Line Projects LLC v. Republic of Yemen*. ICSID Case No. ARB/05/17 (Oman-Republic of Yemen BIT), Award, 223, February 6<sup>th</sup>, 2008: “*As to the cash amount of YR 3,524,326,966 paid under the Settlement Agreement which the present Arbitral Tribunal holds to be internationally ineffective, the Arbitral Tribunal holds that it will take it into consideration when ascertaining the residual amount due by the Respondent.*”

do not.<sup>110</sup> Under BITs, tribunals have ruled on counterclaims for breach of contract or breach of the exact transaction underlying the initial investment claim. BITs do not, however, provide any protections to States for damage arising out of a breach of domestic law, international law, or out of the investment in a capacity not covered by the original claim. The following section outlines the situation and suggests that to the extent that States want these protections, they might want to include additional language to that effect in IIAs.

Tribunals struggle to find space for State counterclaims under BITs. *Mytilineos Holdings SA (Claimant) v. Serbia and Montenegro*, summarized the situation well.<sup>111</sup> “[W]e are dealing here with a unilaterally accepted obligation of the State to appear before an arbitral tribunal in fulfillment of its obligations and responsibilities related to protection of investments by Greek investors. It should be noted that YU/SMO may not initiate arbitral proceedings against a Greek investor –it is even questionable whether it could file a counterclaim.”<sup>112</sup> Recognizing this problem motivated the court to refuse jurisdiction where the investor didn't comply with State law, and to put the burden of proof on the claimant.<sup>113</sup>

The *SGS v. Pakistan* tribunal then identifies the equitable problem.

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110 The first BIT counterclaim, *Genin*, was a justified failure. The tribunal in *Genin* rejected Estonia's counterclaim. According to the tribunal, Estonia the amount and allegations of Estonia's counterclaim varied throughout. See *Alex Genin, Eastern Credit Limited, Inc. & A.S. Baltoil v. Republic of Estonia*. ICSID Case No. ARB/99/2, Award, 376, June 25<sup>th</sup>, 2001. At one point it expressed the counterclaim as “damages in excess of US\$3,400,000 for money illegally diverted from EIB by the Claimants, plus the costs of the arbitration (at 201).”

111 *Mytilineos Holdings S.A. (Claimant) v. Serbia and Montenegro, Serbia*. Ad hoc-UNCITRAL Rules (Greece/Yugoslavia BIT), Partial Award on Jurisdiction, September 8<sup>th</sup>, 2006 and Dissenting Opinion, September 6<sup>th</sup>, 2006.

112 *Mytilineos Holdings S.A. (Claimant) v. Serbia and Montenegro, Serbia*. Ad hoc-UNCITRAL Rules (Greece/Yugoslavia BIT), Partial Award on Jurisdiction, 4, September 8<sup>th</sup>, 2006 and Dissenting Opinion, September 6<sup>th</sup>, 2006.

113 *Mytilineos Holdings S.A. (Claimant) v. Serbia and Montenegro, Serbia*. Ad hoc-UNCITRAL Rules (Greece/Yugoslavia BIT), Partial Award on Jurisdiction, September 8<sup>th</sup>, 2006 and Dissenting Opinion, September 6<sup>th</sup>, 2006. “The fundamental issue posed before the Arbitral Tribunal is, then, to establish whether the Claimant from Greece invested assets in accordance with YU/SMO legislation. The Claimant has failed to prove this, or rather, has not even tried to prove it.”

*The source of jurisdiction to consider such a counter-claim and the governing law applicable to such a claim is of capital importance. It would be inequitable if, by reason of the invocation of ICSID jurisdiction, the Claimant could on the one hand elevate its side of the dispute to international adjudication and, on the other, preclude the Respondent from pursuing its own claim for damages by obtaining a stay of those proceedings for the pendency of the international proceedings, if such international proceedings could not encompass the Respondent's claim.*<sup>114</sup>

BITs and FTAs, as *Mytilineos* highlights, do not provide any explicit protections to States. Conversely, IIAs provide expansive investor protections. “An ICSID tribunal can make determinations based on the contract and on national law in order to decide whether a State has committed a violation of its international law obligations through a breach of the BIT.”<sup>115</sup> All violations must relate to a BIT protection. The *ELSI* case, explains this distinction with respect to violations of municipal law.

*[T]he fact that an act of a public authority may have been unlawful in municipal law does not necessarily mean that that act was unlawful in international law, as a breach of treaty or otherwise. ... In every case it will be seen on analysis that either the provisions of internal law are relevant as facts in applying the applicable international standard, or else that they are actually incorporated in some form, conditionally or unconditionally, into that standard.*<sup>116</sup>

BITs clearly elevate domestic law breaches into international law violations, and thus investors may bring claims for breach of domestic law, but States cannot. As well, BITs guarantee that States will not violate international law with respect to the investment. Investors make no such guarantee to the host State. As a result, where the investor violates international or domestic law –it may not constitute a treaty breach because these treaties provide only investor protections.

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114 *SGS Société Générale de Surveillance S.A. v. Islamic Republic of Pakistan*. ICSID Case No. ARB/01/13, Decision on Jurisdiction, ft 16, August 6<sup>th</sup>, 2003.

115 *SGS Société Générale de Surveillance S.A. v. Islamic Republic of Pakistan*. ICSID Case No. ARB/01/13, Decision on Jurisdiction, ft 16, August 6<sup>th</sup>, 2003.

116 *SGS Société Générale de Surveillance S.A. v. Islamic Republic of Pakistan*. ICSID Case No. ARB/01/13, Decision on Jurisdiction, ft.16, ft. 167, August 6<sup>th</sup>, 2003.

Occasionally, BITs incorporate language defining “*investment*” as an investment in compliance with local laws. But this simply acts as a jurisdictional barrier. Thus, what rights does a State have when an investor breaches an international or domestic law? Where is the hook for a counterclaim that is not based directly on a contract at issue?

### 1. Finding Jurisdiction under a BIT

While IIAs do not provide any explicit protections to States, tribunals have permitted State counterclaims for investor breach of the disputed contract.

#### *Saluka*

*Saluka*, a UNCITRAL case, provides an excellent overview of current State counterclaim jurisdiction. The tribunal finds that “*all disputes*” under Article 8 of the BIT permit counterclaims.<sup>117</sup> However, these counterclaims must be closely related (“*indivisible from*”) to the investor's claim and cannot be based on violations of Czech law.<sup>118</sup> Thus, *Saluka* essentially finds jurisdiction for counterclaims under a BIT, but only with respect to a breach of contract.

Like ICSID, the UNCITRAL Rules provide for State counterclaims.<sup>119</sup> The tribunal found that UNCITRAL Rules coupled with BIT Article 8 language referring to “*all disputes*” extended jurisdiction to State counterclaims.

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117 *Saluka Investments BV v. Czech Republic*. Judgment of the Swiss Tribunal, 39, September 7<sup>th</sup>, 2006, Ad hoc-UNCITRAL Rules; IIC 211 (2006).

118 *Saluka Investments BV v. Czech Republic*. Judgment of the Swiss Tribunal, 65, 67, 79, September 7<sup>th</sup>, 2006, Ad hoc-UNCITRAL Rules; IIC 211 (2006).

119 *Saluka Investments BV v. Czech Republic*. Judgment of the Swiss Tribunal, September 7<sup>th</sup>, 2006, Ad hoc-UNCITRAL Rules; IIC 211 (2006), quoting UNCITRAL Article 19.3: “*In his statement of defence, or at a later stage in the arbitral proceedings if the arbitral tribunal decides that the delay was justified under the circumstances, the respondent may make a counter-claim arising out of the same contract or rely on a claim arising out of the same contract for the purpose of a set-off.*”

*[I]n principle, the jurisdiction conferred upon it by Article 8, particularly when read with Article 19.3, 19.4 and 21.3 of the UNCITRAL Rules, is in principle wide enough to encompass counterclaims. 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.*<sup>120</sup>

To determine jurisdiction under the “*other relevant requirements*,” the *Saluka* tribunal explored Iran-US Claims Tribunal decisions at length. The tribunal compares the “*interdependence and essential unity of the instruments on which the original claim and counterclaim were based*”<sup>121</sup> in successful cases, with unsuccessful cases. Unsuccessful counterclaims occurred where the second agreement was not closely related to the first (even if the underlying investment was the same)<sup>122</sup> or where the alleged breach was not of a contractual obligation.<sup>123</sup> It is worth noting that the Iran-US Claims Tribunal provides a more limited (or at least more explicit definition of) jurisdiction for counterclaims. Tribunals have jurisdiction over “*any counterclaim which arises out of the same contract, transaction or occurrence that constitutes the subject matter of [the] national's claims.*”<sup>124</sup> The tribunal also

120 *Saluka Investments BV v. Czech Republic*. Judgment of the Swiss Tribunal, 39, September 7<sup>th</sup>, 2006, Ad hoc-UNCITRAL Rules; IIC 211 (2006).

121 *Saluka Investments BV v. Czech Republic*. Judgment of the Swiss Tribunal, 69-70, September 7<sup>th</sup>, 2006, Ad hoc-UNCITRAL Rules; IIC 211 (2006): “In American Bell International Group, Inc. v. The Government of the Islamic Republic of Iran et al., 9 the primary claim was based on two contracts. The respondent presented counterclaims based on a different contract between the parties. The tribunal upheld its jurisdiction over the counterclaims: it found that all the contracts involved the same project, and the linkage between them was sufficiently strong so as to make them form one single transaction. A similar conclusion was reached in the Westinghouse Electric Corp. v. The Islamic Republic of Iran et al.”

122 *Saluka Investments BV v. Czech Republic*. Judgment of the Swiss Tribunal, 68-72, September 7<sup>th</sup>, 2006, Ad hoc-UNCITRAL Rules; IIC 211 (2006).

123 *Saluka Investments BV v. Czech Republic*. Judgment of the Swiss Tribunal, 74, September 7<sup>th</sup>, 2006, Ad hoc-UNCITRAL Rules; IIC 211 (2006): “*Other decisions of the Iran-US Claims Tribunal have been to similar effect. The position has been summarised in the following terms: 'When claims are based on contracts, the Tribunal has consistently held that it has no jurisdiction over counterclaims seeking Iranian taxes or social security premiums allegedly owed by the claimant and attributable to the performance of those contracts. The reason is that such counterclaims arise from provisions of Iranian law, not from the contracts. Even when the contracts contained clauses requiring the claimant to comply with Iranian tax and social security laws, it was the law, not the contract, that was the source of the alleged obligation.'*” George H. Aldrich & John K. Aldrich, *The Jurisprudence of the Iran-United States Claims Tribunal*, 116 (Oxford University Press, New York, 1996).

124 *Saluka Investments BV v. Czech Republic*. Judgment of the Swiss Tribunal, 74, September

looks to *Amco* and *Klöckner* for guidance –noting that they require a close connection between the claim and counterclaim, and that *Amco* refused jurisdiction over a counterclaim founded on a breach of domestic law.<sup>125</sup> After reviewing these decisions and the language of UNCITRAL, ICSID, and the Iran-US Claims Tribunal,<sup>126</sup> the tribunal: “*is satisfied that those provisions, as interpreted and applied by the decisions which have been referred to, reflect a general legal principle as to the nature of the close connexion which a counterclaim must have with the primary claim if a tribunal with jurisdiction over the primary claim is to have jurisdiction also over the counterclaim.*”<sup>127</sup>

*Applying this principle the tribunal refuses jurisdiction to all of the Czech Republic's counterclaims. “[I]t is apparent that those heads of counterclaim [D-K] involve non-compliance with the general law of the Czech Republic.”*<sup>128</sup> As well, the tribunal finds that breaches of domestic law do not constitute an “*indivisible whole*” with the primary claim, as found by the *Klöckner* tribunal.<sup>129</sup>

7<sup>th</sup>, 2006, Ad hoc-UNCITRAL Rules; IIC 211 (2006).

125 *Saluka Investments BV v. Czech Republic*. Judgment of the Swiss Tribunal, 75, September 7<sup>th</sup>, 2006, Ad hoc-UNCITRAL Rules; IIC 211 (2006), citing *Amco Asia Corporation, Pan-American Development Ltd. and PT Amco Indonesia v. Republic of Indonesia*. Resubmitted Case, ICSID Case No. Arb/81/1, Decision on Jurisdiction, May 10<sup>th</sup>, 1988.

132 ICSID Reports, 543.

89 *International Law Reports*, ILR 552.

126 *Saluka Investments BV v. Czech Republic*. Judgment of the Swiss Tribunal, 78, September 7<sup>th</sup>, 2006, Ad hoc-UNCITRAL Rules; IIC 211 (2006): “*The Tribunal acknowledges that the several decisions referred to were based on the terms of instruments which differ from those of Article 8 of the Treaty in issue in the present arbitration and of the UNCITRAL Rules ... Nevertheless, Article 19.3 of the UNCITRAL Rules, Articles 25(1) and 46 of the ICSID Convention and Article II(1) of the Iran-US Claims Settlement Declaration, all reflect essentially the same requirement: the counterclaim must rise out of the ‘same contract’ (UNCITRAL Rules, Article 19.3), or must arise ‘directly out of an investment’ and ‘directly out of the subject-matter of the dispute’ (ICSID, Articles 25(1) and 46), or must arise ‘out of the same contract, transaction or occurrence that constitutes the subject matter of [the primary] claims’*”, Article II.1 of the Claims Settlement Declaration.

127 *Saluka Investments BV v. Czech Republic*. Judgment of the Swiss Tribunal, 78, September 7<sup>th</sup>, 2006, Ad hoc-UNCITRAL Rules; IIC 211 (2006).

128 Specifically, “*D alleges violations of Czech banking law and regulations, heads E, H and I allege violations of the Czech Commercial Code, heads F and G allege violations of the Czech Civil Code, and heads J and K allege violations of the Czech law on Protection of Economic Competition*”).

129 *Saluka Investments BV v. Czech Republic*. Judgment of the Swiss Tribunal, 79, September 7<sup>th</sup>, 2006, Ad hoc-UNCITRAL Rules; IIC 211 (2006): “*heads D through K of the Respondent's counterclaim cannot be regarded as constituting (to use the language adopted in Klöckner v. Cameroon, above, paragraph 65) ‘an indivisible whole’ with the primary claim asserted by the Claimant, or as invoking obligations which share with the primary claim ‘a*

## 2. Tribunal willingness

Other tribunals are willing to hear counterclaims under IIAs. IIAs and recourse to early interpretations, like that of Amco, however, may hamper tribunals' ability to uphold counterclaims.

The tribunal in *Sempra*, for example, stated that:

*The Respondent has argued that the Government also had many expectations in respect of the investment that were not met or were otherwise frustrated. Apart from the question of investment risk, it is alleged that there was, inter alia, the expectation that the investor would bear any losses resulting from its activity, work diligently and in good faith, not claim extraordinary earnings exceeding by far fair and reasonable tariffs, resort to local courts for dispute settlement, dutifully observe contract commitments, and respect the regulatory framework. The Tribunal notes that to the extent that any such issues would be within the Tribunal's jurisdiction to decide, and could have resulted in breaches of the Treaty, the Respondent would be entitled to raise a counterclaim. While this right has been resorted to by Respondent States only to a limited extent in cases submitted to ICSID tribunals, nothing prevents its exercise in the light of Article 46 of the Convention and Rule 40 of the Arbitration Rules.*<sup>130</sup>

The tribunal clearly encouraged a counterclaim. However, it simultaneously qualifies its ability to rule on counterclaims. “*To the extent that any such issue would be within the Tribunal's jurisdiction, and could have resulted in breaches of the Treaty, the Respondent would be entitled to raise a counterclaim.*”<sup>131</sup>

The tribunal clearly wishes to provide the State with an equal opportunity to be heard, but the treaty likely provided for very few, if any, substantive protections for a State. Had this tribunal been faced with a counterclaim for “*failure to respect the regulatory framework*” it might have looked at the treaty

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*common origin, identical sources, and an operational unity' or which were assumed for 'the accomplishment of a single goal, [so as to be] interdependent'.* Note that this is dicta in the *Klöckner* tribunal, and is not meant to be exclusive –but rather meant to justify its decision.

130 *Sempra Energy International v. The Argentine Republic*. ICSID Case No. ARB/02/16, Award, 289, September 28<sup>th</sup>, 2007.

131 *Sempra Energy International v. The Argentine Republic*. ICSID Case No. ARB/02/16, Award, 289, September 28<sup>th</sup>, 2007.

language, looked to the resubmitted *Amco* case, and rejected the claim as outside its jurisdiction.

*City Oriente* highlights a similar conundrum.<sup>132</sup> Here, the tribunal denied Ecuador access to payments that they claimed the investor owed under an Ecuadorian Law.<sup>133</sup> In the interest of fairness, the tribunal then stated, “*Respondents may obviously file a counterclaim and, should they succeed, the Tribunal will render an award ordering City Oriente to make payment of all such amounts, which award may be enforced by execution of any of City Oriente's rights and assets in Ecuador.*”<sup>134</sup>

The question, however, is whether the tribunal could honor its offer to Ecuador. Does the tribunal have jurisdiction under the BIT to require the investor to pay local taxes? As well, if the tribunal looks to *Amco* for guidance, it appears that taxes the investor owes under domestic law are generally outside the scope of jurisdiction.

### 3. Suggested Solution

There is a relatively easy solution. States could simply incorporate a clause in all IIAs requiring compliance with domestic and international law.

The clause could be two sentences: “*Investors must comply with international law and the laws of the host State, as well as equitable principles under international law, to the extent that those laws and principles do not represent BIT violations. Any violation of the aforementioned laws constitutes a violation of this agreement.*”

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132 *City Oriente v. Ecuador*. ICSID Case No. ARB/06/21, Decision on Provisional Measures, November 19<sup>th</sup>, 2007.

133 *City Oriente v. Ecuador*. ICSID Case No. ARB/06/21, Decision on Provisional Measures, 59, November 19<sup>th</sup>, 2007: “*Respondents are required to refrain from demanding settlement of such payment or any other amount accrued not on account of the application of the original terms and conditions of the Contract but, rather, of Law No. 2006-42.*”

134 *City Oriente v. Ecuador*. ICSID Case No. ARB/06/21, Decision on Provisional Measures, 59, November 19<sup>th</sup>, 2007.

## V. CURRENT DETERRENCE ALTERNATIVES

Tribunals are addressing the systemic imbalance. Since State counterclaims generally fail, tribunals use jurisdiction. Recent tribunals have refused jurisdiction based on illegality or public policy violations. Some also award the State its legal costs.

*International Investment Arbitration: Substantive Principles* summarizes the current practice with respect to treaty language requiring that protected investments be legal.

*In many investment treaties the definition of 'investment' includes a requirement that the categories of assets admitted as 'investments' must be made 'in accordance with the laws and regulations of the said party.' The plain meaning of this phrase is that investments which would be illegal upon the territory of the host State are disqualified from the protection of the BIT. Attempts by respondent States to broaden the matters encompassed in the phrase have failed.*<sup>135</sup>

*Desert Line*, explored earlier, adds substance. “Moreover, it has been well traversed by arbitral precedents, notably *Inceysa* and *Fraport* which make clear that such references are intended to ensure the legality of the investment by excluding investments made in breach of fundamental principles of the host State's law.”<sup>136</sup>

Other tribunals have refused jurisdiction, with or without treaty references to the legality of the investment. The *Plama* tribunal, for example, concluded that Plama had misrepresented the conditions of investment to Bulgaria. Specifically, the tribunal found deliberate fraud. The tribunal held that the Obligations and Contracts Act of Bulgaria introduced the principle of good faith. The tribunal also understood the Energy Charter Treaty's (ECT) emphasis on the rule of law to preclude investments made contrary to international law. The tribunal would not enforce a contract obtained by wrongful means. Plama's was ordered to

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135 Campbell McLachlan, Laurence Shore & Matthew Weiniger, *International Investment Arbitration: Substantive Principles* (1st ed., Oxford University Press, New York, 2007).

136 *Desert Line Projects LLC v. Republic of Yemen*. ICSID Case No. ARB/05/17 (Oman-Republic of Yemen BIT), Award, 104, February 6<sup>th</sup>, 2008.

pay the fees and expenses of the tribunal and Bulgaria's costs and legal fees, totaling US\$ 7 million.<sup>137</sup> *World Duty Free* similarly denied jurisdiction for breach of public policy, both national and international. In that case, the contract providing for ICSID jurisdiction was obtained through bribery.<sup>138</sup>

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137 *Plama Consortium Limited v. Bulgaria*. ICSID Case No. ARB/03/24 (Energy Charter Treaty), Award, August 27<sup>th</sup>, 2008.

138 *World Duty Free Company Limited v. The Republic of Kenya*. ICSID Case No. ARB/00/7, Award, October 4<sup>th</sup>, 2006.

## CONCLUSION

Tribunals are typically fair. This article is not a criticism of tribunals. The tribunals mentioned have not made any interpretative errors; they have just chosen a particular set of interpretations or been dealt a particular set of facts. Rather, the article observes that between the jurisdictional limitations read into State counterclaims and the scarce protections afforded by IIAs, State counterclaims have failed to effectively enter the ICSID system. State counterclaims might have played and still could play an important role in investor-State disputes. An effort to understand “*consent*” and “*arising out of the subject matter of the dispute*” and “*an investment*” as more inclusive might yield a successful State counterclaim. To the extent, however, that States want the system to truly provide for State counterclaims on a wide swath of issues, States will need to include language requiring that investors respect domestic and international law in the substantive provisions of IIAs, not just when defining investment.

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