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THE ADMISSIBILITY OF ENVIRONMENTAL COUNTERCLAIMS IN INVESTMENT ARBITRATION

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Abstract

The admissibility of environmental counterclaims in investment arbitration is untouched academic territory. The Ecuadorian counterclaims of Perenco *and* Burlington *were the impetus of this analysis. As the first successful environmental counterclaims in investment arbitration, the tribunals' failure to inquire into admissibility warrants further attention. This paper provides an in-depth examination of the gap in this area of investment arbitration. It draws upon international jurisprudence in an attempt to redefine the admissibility inquiry. It concludes that traditional approaches to admissibility will not exclude environmental counterclaims. Requiring a legal connection is an unreasonable and restrictive approach which denies the reality of investment treaties. The asymmetry of such instruments lend host states to rely upon alternative sources of environmental obligations. This should not be fatal to a host State's environmental claim. The nature of environmental claims, including the implication of public policy should not be an impediment for a tribunal to exercise its jurisdiction. So long as an environmental counterclaim has a temporal and geographical connection to the principal claim or arises directly from the investment, there is no reason for it to be inadmissible. In reaching this conclusion, this paper also yields some insight into how host states can increase the receptivity of investment arbitration to environmental matters.*

Keywords

Investment arbitration, environmental obligations, investor obligations, admissibility, counterclaims.

I Introduction

The recent decisions of *Burlington Resources Incorporated v Republic of Ecuador* (*Burlington*) and *Perenco Ecuador Limited v Republic of Ecuador* (*Perenco*) provoke an interesting inquiry. The decisions are unique given they involve the successful pursuit of an environmental counterclaim against an investor. Despite being regarded as a welcomed development in investment arbitration, both decisions failed to consider whether the counterclaims were admissible.[1] This leads us to our central inquiry. To what extent are environmental counterclaims admissible in investment arbitration?

Whether a particular environmental counterclaim, or aspect of a counterclaim, is admissible is a distinct inquiry to that of jurisdiction. The troubled and unpredictable assessment of admissibility is particularly concerning given the increasing breadth of non-commercial matters infiltrating investment disputes. Environmental claims are interesting, given that they are often based on a host State's domestic law and have a character of being regulatory, constitutional and tortious.[2]

This paper will argue that a binary approach to admissibility based on factual and/or connectivity is oversimplified. A holistic, case-by-case approach better caters for the reality that environmental obligations are very rarely included in international investment agreements (IIAs). Accordingly, environmental counterclaims will be admissible when:

(a) They are based on identical legal instruments; or
(b) They are geographically and temporally connected to the principal claim; or
(c) The counterclaim arises directly out of the investment.

Finding the answer to this admissibility question could not be reached by an abstract analysis, a fine-grained approach was required. To this end, this paper will advance in seven substantive parts. Part II will begin by outlining the background to the related *Burlington* and *Perenco* disputes. Part III will introduce the classic paradigm of investment arbitration and why a convincing case for the reverse of this paradigm exists in the context of environmental disputes. This paper is primarily concerned with host state counterclaims. Part IV will explore the concepts of jurisdiction and admissibility. Both are distinct but equally important hurdles a host state must clear for its claim to be heard before a tribunal.

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1 Anagha Sundararajan "Environmental Counterclaims: Enforcing International Environmental Law through Investor-State Arbitration" Salzburg Global Seminar <www.salzburgglobal.org> at 25.

2 Kari-Johanne Iversen "Foreign Direct Liability in Europe for Environmental Damage" (Masters Thesis, University of Oslo, 2013) at 1

Part V will extrapolate the key features of *Burlington* and *Perenco* environmental counterclaims and how these interacted with the investors' principal claims. Given their unique features, it is unlikely these cases will be game changers in the field of investment arbitration. However, they provide insight as to how tribunals may approach environmental claims brought by host states in the future. Part VI will survey international jurisprudence for guidance on the admissibility question. Part VII will make the case for a new approach to admissibility by outlining six key considerations. Part VIII will consider what kinds of environmental claims are likely to be admissible applying the six considerations. Three recommendations will be made as to how host states can promote the arbitration of environmental counterclaims.

This inquiry is of practical importance as it determines the extent to which a host State may resort to arbitration to enforce environmental obligations against investors. This paper proposes a set of guidelines which tribunals can draw upon when considering the admissibility question. While these guidelines are tailored towards environmental claims, they may also be applicable to other areas including the enforcement of human rights and labour rights in investment claims.

II The Ecuadorian Counterclaims

The disputes of *Burlington* and *Perenco* were a response to Ecuador's decision to introduce a 99% "extraordinary profits" tax upon oil companies operating within its jurisdiction in October 2007.[3] Consortium partners, Burlington and Perenco complied with these tax obligations, derived from the production sharing contracts, until June 2008.[4] Thereafter, the consortium refused to meet the payments due and the Ecuadorian government seized the blocks.[5] In April 2008, each brought arbitration claims against Ecuador under the International Centre for Settlement of Investment Disputes (ICSID), relying on the applicable bilateral investment treaty (BIT) and production sharing contract.[6] In 2011, Ecuador brought counterclaims against both investors. Ecuador sought to hold each jointly and severally liable for environmental damage in two oil blocks, Block 7 and Block 21,

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3 *Perenco Ecuador Ltd v Republic of Ecuador (Interim Decision on the Environmental Counterclaim)* ICSID ARB/08/6, 11 August 2015 at [10]; *Burlington Resources Inc. v Republic of Ecuador (Procedural Order No 1 on Burlington Oriente's Request for Provisional Measures)* ICSID ARB/08/5, 29 June 2009 at [8]. [*Burlington* PO 1].

4 *Burlington* PO 1, above n 3, at [9].

5 At [10].

6 *Perenco*, above n 3, at [11]; *Burlington Resources Inc. v Republic of Ecuador (Decision on Ecuador's Counterclaims)* ICSID ARB/08/5, 7 February 2016 at [6]. [*Burlington*].

that had been worked on by the consortium in the Amazon Rainforest.[7] Despite being parallel proceedings, the *Burlington* Tribunal made clear that the arbitrations were separate and would be decided solely on their own record and merits.[8]

In August 2015, the *Perenco* Tribunal issued an interim decision where a final award could only be made following a new expert's examination of the environmental harm.[9] The final decision is still pending. In February 2017, the *Burlington* Tribunal awarded damages of US 41.7 million to Ecuador as the cost of restoring the environment, far less than the US 2.5 billion requested.[10] *Burlington* was one of the first cases in which an investment tribunal awarded compensation on the basis of a host State's counterclaim. It is also notable for the Tribunal's willingness to acknowledge that Ecuador was entitled to seek compensation under its domestic law.[11]

This paper is particularly concerned with the following aspects of the Tribunals' decisions:

(a) the Tribunals' jurisdiction over Ecuador's counterclaim;
(b) the juridical nature of Ecuador's environmental counterclaim;
(c) the source of environmental obligation relied upon by Ecuador;
(d) the type of damage alleged to have been caused by the investors; and
(e) the language of the relevant IIA.

Burlington and *Perenco* tribunals demonstrated a willingness to consider cases that are concerned with issues beyond purely investment and commercial matters. It is interesting that neither tribunal used the language of "admissibility" to assess whether the nature of Ecuador's counterclaims were of the kind which could and should be heard before an investment tribunal.

III The Host State as Claimant

To determine whether environmental disputes brought by a host State should be admissible, one must first understand the context in which such disputes arise. This paper is concerned with the admissibility of environmental disputes in investment arbitration: a dispute

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7 Carol Wood, Ginny Castelan and King & Spalding "Environmental and Human Rights Considerations for International Energy Companies" (paper presented to the Energy Industry Environmental Law Conference, May 2018) at 2.

8 At [69].

9 *Perenco,* above n 3, at [611].

10 *Burlington,* above n 6, at [1199].

11 Sundararajan, above n 1, at 25.

between a host State and an investor. This is distinct from disputes between two states or two private individuals.

A Classic Paradigm

Investment arbitration is commonly perceived as a one-sided game, where it is rare to see a host State file a claim against an investor.[12] In the vast majority of arbitrations, environmental law has been used by host states as a defence to a treaty-based expropriation claim.[13] The typical scenario is where an arbitration is initiated by an investor following the implementation of a new environmental policy by the host State which is thought to have negative ramifications upon the investor's activities.[14] Environmental principles are used to support a host State's right to regulate its environment. This paper is not concerned with how environmental law can be used as a shield by host states. Rather, it is interested in how a host State can enforce environmental law against an investor through arbitration.

The Ecuadorian counterclaims are the only two known arbitrations which involve a successful environmental counterclaim brought by a host State. Why are these kinds of cases so rare? This section is intended to outline why this gap exists. It will begin by explaining the classic paradigm of investor-state arbitration which is attributed to the availability alternative avenues of dispute resolution and the architecture of IIAs. This asymmetry has attracted considerable criticism. There may be instances where alternative avenues are not available or desirable to a host State, particularly in the context of environmental law infamous for lacking adequate enforcement mechanisms. Arbitration should be a feasible alternative for states.

1 Alternative dispute resolution

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12 José Antonio Rivas "ICSID Treaty Counterclaims: Case Law and Treaty Evolution" (2014) 11 TDM 1 at 2.

13 Tamara Slater "Investor-State Arbitration and Domestic Environmental Protection" (2015) 14 Washington University Global Studies Law Review 131 at 147; Vivian Wang "Investor Protection or Environmental Protection? "Green" Development under CAFTA" (2007) 32 Colum J Envtl L 251 at 259.

14 *Metaclad Corporation v The United Mexican States (Award)* ICSID ARB(AF)/97/1, 30 August 2000; *Tecnicas Medioabientales Tecmed v United Mexican States (Award)* ICSID ARB(AF)/00/2, 19 May 2003; *LG&E Energy Corp, LG&E Capital Corp and IG&E International Inc v Argentine Republic (Award)* ICSID ARB/02/1, 3 October 2006. *Methanex Corporation v. United States (Final Award of the Tribunal on Jurisdiction and Merits)* J William, F Rowley, W Reisman, V.V. Veeder 3 August 2005. *S. D. Myers Inc. v Government of Canada (Second Partial Award)* Bryan Schwartz, Edward Chiasson and J Hunter 21 October 2002.

A primary reason for this classic paradigm is that host states have alternative dispute resolution avenues at their disposal. These alternatives may be more advantageous than investment arbitration.[15] They include settling the claim through national courts and having recourse to inter-state dispute resolution. Host states tend to bring environmental claims against investors before their own courts.[16] For example, in 2013 Ecuador brought a claim against Perenco in the Provincial Court of Justice of Orellana for soil contamination in Block 7 in breach of the 2008 Constitution.[17] Sometimes legislation will designate exclusive jurisdiction to national courts.[18] Where this is the case, it must be respected at the transnational level.

The ICJ has played a pivotal role in resolving environmental disputes between states. The *Nicaragua v Costa Rica* case is an example of a state-state dispute. In 2015 Nicaragua initiated proceedings in the International Court of Justice (ICJ) against Costa Rica alleging it had caused "major environmental damages on its territory."[19] The Court ultimately found in favour of Nicaragua as Costa Rica failed to carry out the required environmental impact assessment.[20] This case demonstrates how states can be held liable for harm caused by private actors, despite the obligation not being incorporated into a domestic regime. The limits of pursuing these avenues against an investor will be discussed below.

2 Architecture of IIAs/BITs

The asymmetry of investor-state arbitration is also attributable to the present language and alignment of many IIAs. The failure of IIAs to impose reciprocal obligations upon investors, particular for sustainable development, are at the centre of critiques of foreign

15 Gustav Laborde "The Case for Host State Claims in Investment Arbitration" (2010) 1 JIDS 97 at 98.

16 Jorge Viñuales "The Environment breaks into Investment Disputes" in M Bungenberg, J Griebel, S Hobe and A Reinish (eds) *International Investment Law* (C.H. Beck/Hart/Nomos, Munich, 2012) at 8; Isabel Sarenmalm "Investment Treaty Arbitration and Environmental Sustainability: Are ex officio considerations needed, possible or desirable?" (Master's Thesis in International Investment Law, Uppsala University, 2015) at 28.

17 *Irma A. Imbaquingo v Perenco Ecuador Limited* Exh. CA-CC-57, 17 September 2013.

18 Zachary Douglas "The enforcement of environmental norms in investment treaty arbitration" in Pierre-Marie Dupuy and Jorge E Viñales (eds) in *Harnessing Foreign Investment to Promote Environmental Protection* (Cambridge University Press, Cambridge, 2013) at 434.

19 *Certain Activities Carried Out by Nicaragua in the Border Area (Costa Rica v Nicaragua)* and *Construction of a Road in Costa Rica along the San Juan River (Nicaragua v Costa Rica) (Judgment)* [2015] ICJ Rep 665 at [9].

20 At [168].

investment law.[21] Typically, BITs focus on protecting investors from the exercise of untrammelled sovereign power.[22] Investors are more willing to assume risk when disputes are resolved in an impartial forum.[23] A tribunal's power to adjudicate is usually grounded within the instrument upon which the claim is raised.[24] It is rare for treaties to contain specific obligations owed by investors, especially environmental ones.[25] The very structure of IIAs are asymmetric.[26] This is primarily because host states wish to be seen as "investor friendly".[27] As a result, it is unusual for host states to bring a treaty-based claim.[28] A review of current case law reveals that there have been no disputes initiated by a host State based on an IIA.[29] Throughout the entire history of ICSID arbitration, only four known arbitrations have been initiated by host states.[30]

3 Criticism

Criticism has been levelled at this phenomenon, where host states have adopted the role of 'perpetual respondent'.[31] Investors are accused of using arbitration as a sword against states, when it was intended to be used as a shield. Investors are aggressively using the tool to "attack", rather than for protection.[32] The total cumulative number of known treaty-based

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21 David Hunter, James Salzman and Durwood Zaelke *International Environmental Law and Policy* (2nd ed, Foundation Press, 2009) at 1145.

22 Laborde, above n 15, at 98.

23 Andrew Stephenson and Lee Carroll "The Trans-Pacific Partnership: Lessons Learned for ISDS" in Barton Legum (ed) *The Investment Treaty Arbitration Review* (2nd ed, Gideon Roberton, London, 2017) at 301.

24 Alessandras Asteriti "Environmental Law in Investment Arbitration: Procedural Means of Incorporation" (2015) 15 JWIT 248 at 252.

25 Kathryn Gordon and Joachim Poal "Environmental Concerns in International Investment Agreements: A Survey" (OECD Working Papers on International Investment 2011/01, 2011).

26 Yaraslau Kryvoi "Counterclaims in Investor-State Arbitration" (2012) 21 Minn J Int'l L 216 at 218.

27 Christina Beharry and Melinda Kuritzky "Going Green: Managing the Environment through International Investment Arbitration" (2015) 30 Am U Int'l L Rev 384 at 407.

28 Laborde, above n 15, at 113.

29 "States as Claimants in Investment Arbitration" (23 May 2018) Aceris Law: International Arbitration Law Firm <www.acerislaw.com>

30 Laborde, above n 15, at 97.

31 Mehmet Toral and Thomas Schultz "The State, a Perpetural Respondent in Investment Arbitration? Some Unorthodox Considerations" in Michael Waibel, Asha Kaushal, Kyo-Hwa Liz Chung and Claire Balchin (eds) *The Backlash Against Investment Arbitration: Perceptions and Reality* (Wolter Kulwer, 2010) at 278.

32 Nathalie Bernasconi-Osterwalker *International Legal Framework on Foreign Investment* (Center for International Environmental Law, Background Paper, May 2003) at 6.

cases filed before the end of 2017 surpassed 855, up from 560 in 2013.[33] This proliferation of cases has given rise to a concern that IIAs immunise investors from complying with social and environmental laws by challenging newly implemented policy measures.[34] As a result, host states may feel threatened to adopt policy measures designed to protect the environment or public welfare.

It also appears as though the majority of respondents are developing host states and the majority of claimants are developed-country investors. In 2016, Colombia and India tied first equal as being the most frequent respondent, with four cases against each.[35] In 2016, 27 of 62 known cases were initiated by investors from the Netherlands, the United States and United Kingdom.[36] This asymmetry and inequality undermines the legitimacy of investor-state arbitration as a dispute settlement mechanism.

Many host states have begun to exclude investor-state dispute settlement (ISDS) provisions from treaties or have withdrawn their consent to ICSID jurisdiction over particular matters, such as the environment. In 2007, Ecuador notified the Centre that it would not submit to ICSID's jurisdiction for disputes that arise in matters concerning the exploitation of natural resources.[37] Developed countries have also expressed a degree of hostility towards investment arbitration. Since the election of the Labour-led coalition, New Zealand has opposed the inclusion of ISDS in future free trade agreements.[38] The ISDS provision in the Comprehensive and Progressive Agreement for Trans-Pacific Partnership is qualified by a number of carve-outs and side letters.[39]

The availability of alternative avenues as well as the asymmetry of IIAs provide an explanation for why environmental claims brought by host states are anomalies. However,

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33 Claudia Levy "Drafting and Interpreting International Investment Agreements from a Sustainable Development Perspective" (2015) 3 GroJIL 59 at 60; *World Investment Report 2018* (United Nations Conference on Trade and Development, UNCTAD/WIR/2018, June 2018) at 91.

34 Levy, above n 33, at 60.

35 *World Investment Report 2017* (United Nations Conference on Trade and Development, UNCTAD/WIR/2017, June 2017)

36 *Investor-State Dispute Settlement: Review of Developments in 2016* (United Nations Conference on Trade and Development, UNCTAD/DIAE/PCB/2017/1, May 2017) at 2.

37 Xavier Cadena and Marco Montanes "Introductory Note to Ecuador's Notice Under ICSID Article 25(4)" (2008) 47 ILM 154 at 154.

38 Jacinda Ardern "Foreign speculators house ban" (press release, 31 October 2017).

39 David Parker "New Zealand signs side letters curbing investor-state dispute settlement" (press release, 9 March 2018).

alternative avenues are not always available to host states and recourse to arbitration may be desirable.

B A Role for Arbitration in Environmental Claims

1 Limits of national courts

Recourse to a national court or inter-state dispute settlement mechanism is not always feasible or desirable.[40] For example, it may not be feasible where the claim is based on a legal instrument whose choice of forum clause precludes adjudication by the host State's domestic courts.[41] A similar situation was observed in *Burlington,* where parties entered into a separate agreement whereby Ecuadorian counterclaims could only be filed before the particular arbitration.[42] Recourse to national courts may not be desirable if the host State wishes to avoid its own defective court system or to instil the proceedings with a strong sense of impartiality.[43] Where this is the case, a host State may seek recourse through arbitration.

Judgments of national courts also have enforcement limits in comparison to an award obtained through arbitration.[44] ICSID awards are subject to automatic recognition and receive the same value as a final judgment of a court of any Contracting State.[45] Similarly, the New York Convention provides a safeguard against enforcement, except on seven limited grounds.[46] A host State may elect to pursue arbitration rather than have recourse to its national court purely for the superior international enforcement prospects. The enforcement of awards concerning environmental concerns may be particularly pertinent due to public health and sustainability implications. Arbitration provides a significant advantage in this regard.

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40 Asteriti, above n 24, 271.

41 Laborde, above n 15, at 99.

42 *Burlington,* above n 6, at [61].

43 Charles Brower and Stephan Schill, "Is Arbitration a Threat or a Boon to the Legitimacy of International Investment Law?" (2009) 9 Chi. J. Int'l R 471 at 476.

44 Jacques El-Hakim "Enforcement of Foreign Judgments and Arbitral Awards in Syria" (1990) 5 ALQ 138 at 139.

45 Convention on the Settlement of Investment Disputes between States and Nationals of other States (signed 18 March 1965, entered into force 14 October 1966) 575 UNTS 159, art 54(1). [ICSID Convention].

46 Juliane Oelmann "The Barriers to Enforcement of Foreign Judgments as Opposed to Those of Foreign Arbitral Awards" (2006) 18 Bond LR 77 at 94.

2 Enforcement limits of MEAs

Many multilateral environmental agreements (MEAs) have attracted criticism for articulating "aspirational declarations" and soft goals, rather than explicitly binding states to obligations. Enforcement mechanisms for breach of environmental treaties tend to be vague or lacking entirely.[47] The United Nations Framework Convention on Climate Change in 1992 provided that parties seek "a settlement of [a dispute] through negotiation or any other peaceful means of their own choice."[48] The 2016 Paris Agreement also fails to contain an enforcement mechanism.[49] Failure to explicitly grant jurisdiction to a Court or tribunal creates difficulties for states wishing to enforce obligations.[50]

While private actors have obligations under domestic law, there is no general rule that they are responsible for internationally wrongful acts.[51] Private parties, including investors, are not thought to be bound by obligations in international law.[52] MEAs typically assign obligations to states, not private actors.[53] Only a small number of treaties contain liability of states for environmental harm in relation to particular activities.[54] Furthermore, where the International Court of Justice (ICJ) is stipulated as the enforcement mechanism for a particular MEA, its jurisdiction only extends to states. It does not include applications from or against private entities.[55] The enforcement prospects of international environmental law are limited.

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47 Philippe Sands "Litigating Environmental Disputes: Courts, Tribunals and the Progressive Development of International Environmental Law" (2007) 37 Environmental Policy and Law 66 at 69.

48 United Nations Framework Convention on Climate Change 1771 UNTS 107 (signed 9 May 1992, entered into force 21 March 1994), art 14.

49 Anders Corr "Expect Climate Catastrophe: Paris Agreement Lack Enforcement" (1 December 2016) Forbes <www.forbes.com>.

50 Johanna Rinceanu "Enforcement Mechanisms in International Environmental Law: Quo Vadunt?" (2000) 15 J Envt'l L & Litig 147 at 155.

51 Menno Kamminga *Corporate Obligations Under International Law* (International Law Association, Report of the 71st Conference of the International Law Association, 2004) at 424.

52 Hans Kelsen *Principles of International Law* (Rinehart & Company Inc., New York, 1966) at 194. See a c tritique in André Nollkaemper "Responsibility of Transnational Corporations in International Environmental Law: Three Perspectives" in Gerd Winter *Multilevel Governance of Global Environmental Change: Perspectives from Science, Sociology and the Law* (Cambridge University Press, New York, 2006).

53 Kryvoi, above n 26, at 246.

54 Philippe Sands *Principles of International Environmental Law* (2nd ed, Cambridge University Press, Cambridge, 2003) at 896.

55 "Frequently Asked Questions" International Court of Justice <www.icj-cij.org>.

The classic paradigm is a traditional and misguided belief. It should not blind host states to the ways in which they can rely upon legal instruments to bring a claim against investors in arbitration. It is time to seriously consider the possibility of proceedings that go both ways.

C Reversing the Paradigm

1 The rationale

The rationale for allowing claims by host states lies in procedural economy and the better administration of justice.[56] Prior to bringing a counterclaim or on rejection of a counterclaim, a host State may seek relief in its own courts or in an alternative dispute resolution forum. This is likely to be inefficient,[57] expensive and could result in a contradictory decision.[58] Ben Hamida states:[59]

> The exclusion of counterclaims results in a higher number of proceedings and creates difficult problems of *lis pendens* and connexity. On the other hand, the acceptance of these counterclaims provides both a better administration of justice and judicial economy and it allows arbitrators to have an overview of the respective claims of the parties and to decide disputes in a more consistent fashion.

It may be in the best interests of both parties to consolidate a claim. However, counterclaims are rather limited in their usefulness as *ex post facto* remedies.[60] The investor must bring a claim for some type of harmful conduct on the part of the host State. The ready availability of counterclaims may encourage host states to seek conflict with investors. Counterclaims are only one route through which a host State could pursue an environmental claim against an investor. A host State may be able to submit a principal claim as an alternative. Although this option may be less common due to jurisdictional and procedural limitations.[61]

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56 Andrea K. Bjorklund "The Role of Counterclaims in Rebalancing Investment Law" (2013) 17 LCRL 461 at 475.

57 Hege Kjos *Applicable Law in Investor-State Arbitration: The Interplay between National and International Law* (Oxford University Press, New York, 2013) at 26

58 At 131.

59 Walid Hamida, "L'arbitrage Etat-investisseur cherche son équilibre perdu: Dans quelle mesure l'Etat peut introduire des demandes reconventionnelles contre l'investisseur prive?" (2005) 7 International Law Forum du droit international 261 at 270-271.

60 Jose Daniel Amado, Jackson Shaw Kern and Martin Doe Rodriguex *Arbitrating the Conduct of International Investors* (Cambridge University Press, Cambridge, 2018) at 118.

61 Laborde, above n 15, at 101.

2 Bilateral application of ICSID

Equality of access was envisaged by the very institution which has brought arbitration much of its success as a dispute resolution forum. The ICSID Convention recognises the ability of host states to enforce investor obligations directly by bringing a principal claim as claimant or indirectly through a counterclaim as respondent.[62]

> [T]he 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.

Unfortunately, this idea of equal access has failed to come to fruition for the reasons above.[63] The ICSID Convention and UNCITRAL Rules also outline a process for counterclaims. Despite the traditional understanding of investor-state arbitration, the institutional framework envisages greater reciprocity.

3 A new generation of BITs

A decade ago Judge Stephen Schwebel argued that the concept of the classic paradigm is "as colourful as misconceived".[64] Schwebel recognised that some treaties did provide for substantive obligations owed by investors enabling a host State to bring a claim as claimant.[65] This is especially the case in recent years which has observed a wave of new generation IIAs.[66]

Article 14 of the 2005 International Institute of Sustainable Development Model Agreement requires an investor to abide by domestic law and parts of international law, including the precautionary principle in the pre-investment environmental impact assessment.[67] This model treaty also includes procedural clauses permitting counterclaims and expressly allows for host states to initiate proceedings against an investor for breaches

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62 ICSID Convention, art 13.

63 Laborde, above n 15, at 100.

64 Stephen Schwebel "A BIT about ICSID*"* (2008) 23 Foreign Investment LJ 1 at 5.

65 Wolfgang Alschner and Elisabeth Tuerk "The Role of International Investment Agreements in Fostering Sustainable Development" in Freya Baetens (ed) *Investment Law within International Law* (Cambridge University Press, New York, 2016) at 220.

66 Levy, above n 33, at 83.

67 Howard Mann, Konrad von Moltke, Luke Peterson and Aaron Cosbey *International Institute for Sustainable Development Model International Agreement on Investment for Sustainable Development* (International Institute for Sustainable Development, 2005) at 9-11.

of the particular articles of the agreement included in the section on investor's duties.[68] In 2015 UNCTAD released the Investment Policy Framework for Sustainable Development. This resource is intended to facilitate the development of a new generation of IIAs which emphasise the importance of including reciprocal obligations which promote responsible investment.[69]

Aside from treaty-based obligations, it is also common to find investors obligations contained in the investment contract,[70] the domestic law of the host State[71] and occasionally in international law.[72] As *Burlington* and *Perenco* demonstrated, it is possible to rely upon alternative bases to enforce these obligations in arbitration.

Academic literature has failed to discuss the admissibility of a host State's claim found upon alternative sources, such as tort, constitutional law or domestic regulations. This was the case in *Burlington* and *Perenco*. Reliance upon these sources may invite an investment tribunal to adjudicate upon subject matters which raise public interest concerns and may interfere with the regulatory power of states.[73] In the context of environmental protection, it is this gap this paper seeks to fill.

For a host State that wishes to raise a direct claim or a counterclaim against an investor for breach of an environmental obligation there are two distinct challenges. First, establishing the tribunal's jurisdiction to hear the claim. Second, establishing the admissibility of a claim to be heard in arbitration. Often used interchangeably, these barriers are conceptually distinct which warrant independent analysis.

IV Admissibility v Jurisdiction

A The Distinction

A host State that wishes to bring an environmental counterclaim will encounter preliminary hurdles of jurisdiction and admissibility. Commentators have conveyed frustration that the

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68 At 11.

69 United Nations Conference on Trade and Development "Investment Policy Framework for Sustainable Development (UNCTAD/DIAE/PCB/2015/5, 2015) at 77.

70 Douglas, above n 18, at 434.

71 Model Text for the Indian Bilateral Investment Treaty 2016, art 12.

72 Mann, von Moltke, Peterson and Cosbey, above n 69, at 14.

73 Levy, above n 33, at 79.

issues have been too eagerly conflated.[74] There continues to be inconsistent uses of the terms across various fields of international dispute resolution.[75] For instance, what may be an admissibility issue in international litigation, may be categorised as a jurisdictional issue in investment arbitration.[76] In investment arbitration the boundaries between jurisdiction and admissibility are a 'twilight zone'.[77] Attributing concise definitions to such "elusive" concepts is challenging at best, but an attempt should be made.[78]

Jurisdiction refers to the capacity of a tribunal to hear a dispute brought before it by the parties.[79] Comparatively, the concept of admissibility is an objection to the particular kind of claim being brought to a tribunal. [80] In his dissenting opinion in *Waste Management Inc v United Mexican States*, Keith Highet put the distinction quite simply that, "jurisdiction is the power of the tribunal to hear the case; admissibility is whether the case itself is defective – whether it is appropriate for the tribunal to hear it."[81] While the distinction is easily comprehendible in theory, its application is problematic.

The significance of the distinction cannot be understated. As Paulsson observed, decisions on jurisdiction can be overturned on review, however determinations on admissibility are final.[82] Where an issue of admissibility is incorrectly categorised as a jurisdictional issue this may result in an unwarranted extension of the scope for challenging an award. This

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74 Gerold Zeiler "Jurisdiction, Competence, and Admissibility of Claims in ICSID Arbitration Proceedings" in Christina Binder, Ursula Kriebaum, August Reinisch and Stephan Wittich (eds) *International Investment Law for the 21st Century: Essays in Honour of Christoph Schreuer* (Oxford University Press, 2009) at 82; Cameron Miles "Corruption, Jurisdiction and Admissibility in international Investment Claims" (2012) 3 Journal of International Dispute Settlement 329 at 338.

75 Andrew Newcombe "The Question of Admissibility of Claims in Investment Treaty Arbitration" (3 February 2010) *Kluwer Arbitration Blog* <arbitrationblog.kluwerarbitration.com>.

76 Michael Waibel "Investment Arbitration: Jurisdiction and Admissibility" (University of Cambridge, Paper No. 9/2014, February 2013) at 8.

77 Jan Paulsson, 'Jurisdiction and Admissibility' in Gerald Aksen, Karl-Heinz Böckstiegel, Paolo Michele Patocchi and Anne Marie Whitesell (eds) *Global Reflections on International Law, Commerce and Dispute Resolution: liber amicorum in honour of Robert Briner* (ICC Publishing, Paris, 2005) at 601–617.

78 Zeiler, above n 74, at 81.

79 Miles, above n 74, at 334.

80 Hanno Wehland "Jurisdiction and Admissibility in Proceedings under the ICSID Convention and the ICSID Additional Facility Rules" in Crina Baltag (ed) *ICSID Convention after 50 Years: Unsettled Issues* (Wolters Kluwer, 2017) at 232.

81 *Waste Management Inc v United Mexican States (Dissenting Opinion (of Keith Highet))* ICSID ARB(AF)/98/2, 8 May 2000 at [58].

82 Laurent Gouiffes and Melissa Ordonez "Jurisdiction and admissibility: are we any closer to a line in the sand?" (2015) 31 Arb Intl 107 at 108.

procedural distinction is also important given that admissibility questions are considered as part of the merits, albeit preliminary and procedural in character.[83] Unlike an analysis of admissibility, an examination of jurisdiction can occur without assessing the merits. A culpable respondent may use this to its advantage: jurisdictional challenges can be a clever distraction.[84]

It is also worth noting the concept of arbitrability. Arbitrability is thought to concern whether a "specific class of disputes are exempt or suitable to be settled by arbitration".[85] This paper avoids using arbitrability as a measure of whether a host State's claim can be properly brought before an investment tribunal. This is primarily because the concept is not fixed and attempts to define its parameters have been largely in the context of defences to particular investor claims.[86]

This analysis is concerned with admissibility. Demarcating between questions of jurisdiction and admissibility is necessary before any attempt can be made to identify a non-exhaustive set of admissibility factors.

B Jurisdiction

A host State that wishes to bring a counterclaim will encounter a jurisdictional barrier. Although not the fulcrum of this paper, it is still necessary to address this hurdle which states must clear to successfully bring a claim against investors. Hence, this section is to provide a brief descriptive outline and preface the main areas of contention which are not necessary to address further.

The authority of a tribunal to hear a dispute is derived from the parties' consent.[87] It is obtained by interpreting the arbitration clause and the arbitration rules governing the proceedings.[88] Some treaties explicitly allow for either disputing party to bring a claim or provides for counterclaims.

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83 Miles, above n 74, at 339.

84 At 338.

85 Johan Billiet *International Investment Arbitration: A Practical Handbook* (Maklu Publishing, Portland, 2016) at 195.

86 Natalja Freimane "Arbitrability: Problematic Issues of the Legal Term" (Masters Thesis, Riga Graduate School of Law, 2012) at 14.

87 Levy, above n 33, at 79.

88 Pierre Lalive and Laura Halonen "On the Availability of Counterclaims in Investment Treaty Arbitration" (2011) 2 Czech YB of Intl L 141 at 144; Asteriti, above n 24, at 257.

There is a general consensus that tribunals have jurisdiction over counterclaims, unless explicitly excluded in the applicable instrument.[89] Where parties couch their consent to arbitration in broad terms, there is nothing in principle standing in the way of a tribunal exercising its jurisdiction over counterclaims.[90] Most treaties have purposely broad language, giving a tribunal jurisdiction over "any legal dispute" arising from the investment.[91] The Argentina-Spain BIT in *Urbaser v Argentina* expressly provided that a dispute could be submitted to arbitration "at the request of either party". The BIT was neutral as to the identity of the claimant or respondent.[92] Conversely, other treaties may restrict jurisdiction to particular substantive protections.[93] The Cyprus-Hungary BIT limits disputes to expropriation claims.[94] In this instance, a tribunal would not have jurisdiction over a host State's environmental counterclaim.

Whether a tribunal can exercise its jurisdiction over a host State counterclaim also depends upon the arbitration rules that govern the procedure. The applicable rules are art 46 of the ICSID Convention and art 21 of the UNCITRAL Arbitration Rules. Both rules explicitly confirm the availability of counterclaims subject to particular jurisdictional and admissibility requirements. According to art 46 of the ICSID Convention:

> 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.

Article 21(3) of the UNCITRAL Rules 2010 states:

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89 James Harrison "Environmental Counterclaims in Investor-State Arbitration" (2016) 17 JWIT 479 at 486. Douglas, above n 18, at 434.

90 Zachary Douglas *The International Law of Investment Claims* (Cambridge University Press, New York, 2012) at 256.

91 Agreement between the Government of the Republic of France and the Government of the Republic of Ecuador ensuring the Reciprocal Encouragement and Protection of Investments (signed 7 September 1994, entered into force 10 June 1996). [France-Ecuador BIT].

92 *Urbaser S.A.and Consorcio de Aguas Bilbao Bizkaia, Bilbao Biskaia Ur Partzuergoa v The Argentine Republic (Award)* ICSID ARB/07/26 8 December 2016 at [1143].

93 Asteriti, above n 24, at 252.

94 Agreement between the Government of the Republic of Cyprus and the Government of the Hungarian People's Republic of Mutual Promotion and Protection of Investments (Cyprus-Hungary) (signed on 25 May 1989, entered into force 25 May 1990) art 7.

> In its statement of defence, or at a later stage in the arbitral proceedings if the arbitral tribunal decides that the delay was justified under the circumstances, the respondent may make a counterclaim or rely on a claim for the purpose of a set-off provided that the arbitral tribunal has jurisdiction over it.

While consent and connectivity are concurrent requirements for a tribunal to exercise its jurisdiction over counterclaims, they can be categorised differently. Consent is a jurisdictional issue as the tribunal's jurisdiction rests upon agreement of the parties.[95] The connectivity requirement exists in addition to jurisdictional requirements. This suggests that the inquiries are distinct. Connectivity is not required to establish jurisdiction. Any inquiry concerning factual or legal connectivity is a question of admissibility.[96] Furthermore, art 80 of the ICJ Rules clearly delineates between jurisdiction and connectivity.[97] This categorisation is supported by the Tribunal in *Metal-Tech v Ubekistan* which observed:[98]

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

Where a host State's counterclaim is based upon contract, satisfying the consent requirement is relatively straightforward.[99] An issue arises where the claim is based upon a treaty.[100] The scope of consent has not been mutually agreed upon by the parties.[101] The offer to arbitrate is made by the host State when the agreement comes into force.[102] The offer is only perfected when an investor files a notice to arbitrate.[103] This is referred to as "arbitration without privity".[104] A restrictive interpretation would exclude the possibility

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95 Kamran Musayev "Counterclaims in treaty-based investment arbitration: an analysis of two main requirements for their admission" (Masters Thesis, University of Oslo, Faculty of Law, 2017) at 7.

96 Ryan Smith "The Green Retort: The limitation of the procedural basis for counter-claims and its effect on environmental counter-claims" (9 February 2018) LinkedIn <www.linkedin.com>.

97 Rules of the International Court of Justice (adopted 14 April 1978, entered into force 1 July 1978), art 80. [ICJ Rules].

98 *Metal-Tech Ltd v Republic of Uzbekistan (Award)* ICSID ARB/10/3, 4 October 2013 at [407].

99 Beharry and Kuritzky, above n 27, at 408.

100 Lalive and Halonen, above n 88, at 150.

101 At 12.

102 Hege Veenstra-Kjos "Counterclaims by Host States in Investment Treaty Arbitration" in P Kahn and T Walde (ed) *Les aspects nouveaux du droit des investissements internationaux: les livres de droit de l'Academie (New Aspects of International Investment Law: The Law Books of the Academy*) (Nijhoff, Leiden, 2007) at 600.

103 Asteriti, above n 24, at 258.

104 Jan Paulsson "Arbitration Without Privity" (1995) 10 ICSID Review Foreign Investment Law 232.

of direct claims and counterclaims raised by a host State.[105] If a host State wished to allow the possibility of counterclaims it should have explicitly done so in the IIA.[106] This is an unreasonably narrow interpretation. A wider and fairer interpretation should require an express agreement between parties should they wish to exclude the possibility of counterclaims.[107]

In *Burlington*, the Tribunal's jurisdiction in relation to Ecuador's counterclaim was not challenged.[108] This case is unusual as Burlington consented to the Tribunal's jurisdiction over Ecuador's counterclaims.[109] This was to "ensure maximum judicial consistency".[110] The Parties also agreed that Ecuador waived its right to file the counterclaims against Burlington before "any jurisdiction… except this Arbitration."[111] The Tribunal had no issues in satisfying consent.

In *Perenco*, Ecuador presented its counterclaims pursuant to Rule 40 of the ICSID Rules, which is identical to Article 46 of the ICSID Convention.[112] The Tribunal did not provide any discussion justifying it exercising jurisdiction over the counterclaims. This may be because the France–Ecuador BIT identified the Tribunal's jurisdiction to hear "any legal dispute… concerning the investment."[113] This clause is particularly wide. If it were the basis for the Tribunal's jurisdiction, this may have opened the floodgates for host state counterclaims. A more likely explanation is that the BIT was taken in conjunction with Rule 40 of the ICSID Rules allowing counterclaims.[114] If this is so, *Perenco* offers limited grounds for host states that attempt to bring counterclaims, particularly due to the broad language of the France-Ecuador BIT.

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105 Christoph Schreuer, Loretta Malintoppi, August Reinisch and Anthony Sinclair *The ICSID Convention – A Commentary* (2nd ed, Cambridge University Press, 2009) at 751.

106 *Spyridon Roussalis v Romania (Award)* ICSID ARB/06/1, 7 December 2011 at [759].

107 Mark Bravin and Alex Kaplan "Arbitrating Closely Related Counterclaims at ICSID in the Wake of *Spyridon Roussalis v Romania*" (2012) 9 TML 1 at 6.

108 *Burlington,* above n 6, at [60].

109 At [61]; Elena Burova "Jurisdiction of Investment Tribunals over Host States' Counterclaims: Wind of Change?" (6 March 2017) Kluwer Arbitration Blog <arbitrationblog.kluwerarbitration.com>.

110 *Burlington,* above n 6, at [60].

111 At [61].

112 ICSID Convention, r 40.

113 France-Ecuador BIT, art 9.

114 Harrison, above n 91, at 486.

Consent to counterclaims remains a controversial issue, especially in treaty-based arbitration. Given the novel situation in *Burlington* and lack of reasoning in *Perenco* the jurisdictional hurdle of bringing an environmental counterclaim remains unclear.

C Admissibility

Admissibility is not mentioned in the ICSID Convention, the ICSID Rules or the UNCITRAL Arbitration Rules. There is no sight of it in NAFTA, the Energy Charter Treaty nor in the majority of IIAs.[115] Those that do mention it, fail to define it.[116] The lack of definition is concerning as the concept is frequently referred to in the jurisprudence constante in international litigation, particularly in the ICJ relating to claims of diplomatic protection.[117] Having assumed jurisdiction, inadmissibility enables international courts to refuse to exercise that jurisdiction and consequently preclude any decision on a claim's merits.[118]

Parry and Grants Encyclopedic Dictionary of International Law describes the concept as:[119]

> [t]he requirements laid down by customary international law or by treaty (eg as to nationality of claims or exhaustion of local remedies) which an applicant before an international tribunal must fulfil if the tribunal, although it has jurisdiction to hear the case, is able to determine the merits.

Newcombe argues that investment arbitral tribunals can rely on rules of admissibility when deciding whether a claim can be heard.[120] Enabling a tribunal to do this is not so clear cut. Given that ICSID and UNCITRAL do not mention the concept, it could be argued that unless the IIA explicitly endorses admissibility, the tribunal can consider the merits as soon as jurisdiction is established.[121] The tribunal in *Methanex v United States* adopted this view,

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115 Wehland, above n 82, at 232.

116 Saar Pauker "Admissibility of claims in investment treaty arbitration" (2018) 34 Arbitrational International 1 at 2.

117 Miles, above n 74, at 335.

118 Pauker, above n 116, at 2.

119 Clive Parry, John Grant and Craig Barker *Parry and Grant Encyclopaedic Dictionary of International Law* (2nd ed, Oceana Publications Inc, 2003) at 423.

120 Newcombe, above n 77, at 1.

121 At 1.

"[t]his Tribunal has no express or implied power to reject claims based on inadmissibility. Accordingly, we reject the US's admissibility challenges generally."[122]

Despite the weight of the proposition above, it is respectfully submitted that for both practical and legal reasons a tribunal should be able to consider questions of admissibility. There are two key reasons for this. First, the considerable cross-over between treaty arbitration and public international law mandates a tribunal to apply other sources of law beyond the treaty itself. These include fundamental customary international law rules and general accepted principles of law.[123] Second, considering questions of admissibility provides for greater flexibility and a more balanced approached. The current reluctance to assess admissibility risks "drawing a formalistic line of demarcation, which may in practice give rise to random results."[124]

This paper accepts that admissibility considerations are relevant. The question becomes what are the features of an inadmissible claim?[125] To some extent, we can only categorise a dispute as inadmissible on the occasions they arise.[126] Defining the scope of admissibility has not appeared to be particularly significant to early tribunals faced with the inquiry. This has only exacerbated the vacuum of scholarship in this area. There is clear consensus that admissibility covers a wide range of matters including:[127]

(a) Connectivity with the principal claim;[128]
(b) Issues in relation to standing;[129]
(c) Issues relating to the judicial/arbitral function;
(d) Mootness of the claim;[130]
(e) Fork in the road clause;[131]

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122 *Methanex Corporation v United States of America (Partial Award (Preliminary Award on Jurisdiction and Admissibility))* PCA 7 August 2002 at [126].

123 Pauker, above n 116, at 68.

124 At 67.

125 August Reinisch "Jurisdiction and Admissibility in International Investment Law" (2017) 16 The Law and Practice of International Courts and Tribunals 21 at 43.

126 Janet Walker "Arbitrability: Are there Limits" (paper presented at the LCIA Symposium, Montreal, October 2004) at 2.

127 Waibel, above n 76, at 8.

128 Kjos, above n 57, at 147; Lalive and Halonen, above n 88, at 145.

129 Robert Kolb *The International Court of Justice* (Hart Publishing, Oxford, 2013) at 203.

130 Andreas Zimmerman, Christian Tomuschat, Karin Oellers-Frahm and Christian Tams *The Statute of the International Court of Justice: A Commentary* (2nd ed, Oxford University Press, Oxford, 2012) at 12.

131 Pauker, above n 116, at 2.

(f) Exclusion jurisdiction; and
(g) Failure to exhaust local remedies.[132]

Article 46 of the ICSID Convention prescribes a connectivity requirement. It requires the dispute to "arise out of the same subject matter". Whether this requires a factual or legal connection has caused considerable debate.[133] The interpretation of art 46 has significant practical implications.

The Tribunal in *Burlington* satisfied art 46 of ICSID, therefore the following conditions were met: the counterclaims arose directly out of the subject matter of the dispute; they were within the scope of the Parties consent; and, they fell within the Tribunal's jurisdiction circumscribed by art 25.[134] It is interesting that the Tribunal did not inquire into whether the counterclaim was based on the same legal instrument. This is contrary to the decision in *Saluka* and suggests that the Tribunal construed the 'connection' prerequisite to require a factual nexus, as opposed to a legal nexus.[135] If the Tribunal pursued a juridical connectivity requirement, the environmental counterclaim would have failed. This is because Ecuador's claims were based upon domestic law, as opposed to the treaty and production sharing contracts which were the foundations of Burlington's principal claim.[136] The Tribunal in *Burlington* appeared to require a factual connection. This is supported by the official "Notes" that supplemented the original version of the ICSID Arbitration Rules:[137]

> The test to satisfy this condition is whether the factual connection between the original and the ancillary claim is so close as to require the adjudication of the latter in order to achieve the final settlement of the dispute …

The *Burlington* Tribunal's observation may have significant implications for establishing whether an environmental claim is admissible to arbitration in the future.

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132 Reinisch, above n 125, at 30.
133 Smith, above n 96.
134 *Burlington*, above n 6, at [62].
135 *Saluka v Czech Republic (Decision on Jurisdiction over the Czech Republic's Counterclaim)* PCA 7 May 2004 at [76]; Smith, above n 96.
136 Smith, above n 96.
137 International Centre for Settlement of Investment Disputes (1968) ICSID/4/Rev 1 at 105.

Article 21 of the UNCITRAL Rules does not mention a connectivity requirement. Prior to the 2010 amendment art 19(3) of the original UNCITRAL Rules 1976 read:[138]

> …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 (emphasis added).

This previous reference to "contract" was incompatible with investment treaty arbitration.[139] Where there was no investment contract, a host State forfeited its right to bring a counterclaim under UNCITRAL. A wider reading was preferred to interpret "contract" as really meaning "investment".[140] The Drafting Committee for the UNCITRAL Rules proposed that "arising out of the same contract" be replaced with "arising out of the same dispute, transaction or subject matter".[141] This suggests the Committee intended to significantly widen the scope of counterclaims. This proposal was rejected. Instead, the 2010 amendment elected not to include a connectivity requirement at all. This omission solves the quandaries associated with arbitrations which arose under international treaties.[142] It also suggests that connectivity should not be determinative of admissibility.

The question of admissibility is important, especially as investment tribunals are required to adjudicate upon matters transcending purely commercial disputes more often. It is not merely a semantic or theoretical exercise. This paper will critically analyse whether the question of admissibility can include other considerations including when a host State counterclaim is based upon:

(a) tort, regulatory or constitutional law;
(b) public law, for instance tax or penal codes;
(c) international law norms, for instance environmental norms; or
(d) engages significant public policy concerns.

Identifying these features is a crucial step in addressing the fundamental question posed in this paper: what kind of environmental claims are admissible before an arbitral tribunal?

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138 United Nations Commission on International Trade Law Arbitration Rules 15 ILM 701 (1976) (entered into force 15 December 1976).

139 Musayev, above n 95, at 25.

140 Douglas, above n 90, at 494.

141 Report of the United Nations Commission on International Trade Law: Summary of Discussion of the Preliminary Draft (1975) 6 Yearbook of UNCITRAL at 38.

142 Lalive and Halonen, above n 88, at 145.

V Burlington and Perenco

The Ecuadorian counterclaims provide unique insight into how an investment tribunal may treat future environmental claims brought by a host State against an investor. The background to the disputes was discussed in Part II. The jurisdictional question was discussed in Part IV. This section is dedicated to a proper analysis of the juridical character of Ecuador's cause of action, its connection with the investors' principal claim, the sources of law applied, as well as how the tribunal went about making its decision. Despite being separate ICSID arbitrations, Ecuador's counterclaims against Burlington and Perenco rest upon the same facts and legal arguments.

A Ecuador's cause of action

Ecuador's counterclaim rested upon the investors' strict liability for environmental damage, including significant soil and groundwater pollution, found in Blocks 7 and 21.[143] Ecuador sought $2.8 billion in damages for soil and groundwater remediation, groundwater studies and the abandonment of wells.[144] The claim was based solely upon Ecuadorian tort law, as opposed to contract law.[145] Ecuador made this clear: "…our case is not based upon any contractual liability, but rather of a tort liability".[146]

Ecuador explained its approach:

> "[b]ecause Ecuadorian law recognizes the principle of strict liability for environmental damages caused by hydrocarbons operations, there is no need to consider separately whether, in addition, Burlington could be contractually liable to Ecuador for that same environmental damage under the Participation Contracts […]"

Despite the clear statement that cause of action was based entirely upon tort law, Ecuador attempted to rely upon the production sharing contracts (PSCs) to supplement its claim to extend the temporal scope of the strict liability regime.[147] The Tribunal refused to resort to the PSCs as the 2008 Constitution and Ecuadorian case law provided the applicable tort liability principles.[148]

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143 *Burlington*, above n 6, at [52].
144 At [52]; *Perenco*, above n 3, at [36].
145 *Burlington*, above n 6, at [73].
146 At [259].
147 At [258[.
148 At [262].

Ecuador relied upon the 2008 Constitution which establishes strict liability for environmental harm and full reparation.[149] It is clear from Ecuador's approach that it was trying to pursue its constitutional obligation to vindicate any environmental harm caused by Burlington and Perenco.[150] Ecuador's main claims included that:

(a) Burlington is strictly liable for all environmental harm found in Blocks 7 and 21;[151]
(b) The 2008 Constitution applies to damage discovered after its entry into force;[152]
(c) Environmental claims are imprescriptible;[153]
(d) Burlington must fully restore damaged environment to background values or to sensitive ecosystems standard.[154]

Despite arising from the Consortiums' investments, Ecuador's counterclaims have no legal connection with Burlington and Perenco's principal claims. The principal claims were based upon Ecuador's alleged breach of art II and III of the Treaty [between the United States and the Republic of Ecuador concerning the Encouragement and Reciprocal Protection of Investment].[155] Firstly, that Ecuador unlawfully expropriated Burlington's investment in Ecuador.[156] Secondly, that Ecuador failed to accord Burlington's investment with fair and equitable treatment, full protection and security and treatment no less favourable than that required by international law.[157] It was also alleged that Ecuador breached each of PSCs.[158] As referred to in the previous discussion on admissibility, there is no legal connection present. It is possible to ascertain a factual connection between the claims. The environmental damage caused by the investors were temporally and geographically related to the investment and the investors' principal claims. Both occurred with respect to the investors' oil drilling in the Amazonian forests between 2003 and 2009. The Tribunal may have oversimplified the inquiry. It took Burlington's consent to counterclaims as satisfying both the jurisdictional consent requirement and the

149 Republic of Ecuador Constitution 2008 (Ecuador), art 11.3 and 395. [Constitution of Ecuador].
150 *Burlington,* above n 6, at [80].
151 At [81].
152 At [83].
153 At [85].
154 At [99].
155 *Burlington* PO 1, above n 3, at [16].
156 At [16].
157 At [16].
158 At [16].

admissibility requirement of connectivity. In the alternative, the Tribunal may have applied a factual connectivity test but failed to discuss its reasoning.

B Applicable law

It was undisputed that Ecuadorian law applied to the substance of both disputes. Article 42(1) of the ICSID Convention states that the Tribunal shall decide the dispute "in accordance with such rules of law as may be agreed by the parties", absent which "the Tribunal shall apply the law of the [host State]… and such rules of international law may be applicable."[159] Block 7 and 21 PSCs stipulated that the Contractor agreed to comply with "all laws, regulations and other provisions" of Ecuador that are applicable to the contracts.[160] Neither party argued that the choice of Ecuadorian law encompassed torts. However, the tribunal applied Ecuadorian tort law as the law of the host State under the second limb of art 42(1). This meant that international law may have also applied at the discretion of the Tribunal.

Ecuador's reliance upon the 2008 Constitution is a unique feature of these decisions. As recognised by the *Burlington* Tribunal, environmental protection is a "fundamental pillar" of the 2008 Constitution.[161] Environmental stewardship appears to have taken on a new meaning in Ecuadorian society.[162] Nature itself, receives rights and constitutional protections – in Andean terms, Pacha Mama.[163] Environmental sustainability and protection are declared as a matters of public interest.[164] Article 72 encapsulates this special treatment:[165]

> Nature has the right to be restored. This restoration shall be apart from the obligation of the State and natural persons or legal entities to compensate individuals and communities that depend on affected natural systems.

These special rights have also been manifested in the PSCs which Ecuador relied upon as supplementary legal instruments, albeit not forming the basis of the claim. Clause 5.1.20 of the Block 7 PSC stipulates that the Contractor agreed to "preserve the existing ecological

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159 ICSID Convention, art 42(1).

160 *Burlington*, above n 6, at [218].

161 At [216].

162 At [216].

163 At [216].

164 At [233].

165 Constitution of Ecuador, art 72.

equilibrium in the Contract Area" in accordance with all pertinent standards and the environmental impact studies.[166] The Contractor also accepted to "[t]hroughout the term of this Contract, take all necessary measures to conserve and safeguard life and property and to protect the environment."[167] There is no doubt that Burlington and Perenco owed these environmental obligations to Ecuador.

C Tribunal's reasoning

The *Perenco* Tribunal's Interim Decision outlines the two most important issues it was faced with. First, the relationship between the Constitution's full restoration standard and the regulatory permissible limits standard. Second, whether the Constitution's strict liability standard could be applied to the investors' activities prior to the Constitution's entry into force in October 2008.[168] Identical issues were dealt with by the *Burlington* Tribunal. The *Burlington* Tribunal's decisions on these matters echo that of the *Perenco* Interim Decision.

Both tribunals sided with the investors on the first issue. The tribunals concluded that the correct measure of restoration was that according to the detailed statutory and regulatory provisions in Ecuadorian law.[169] The full restoration or "background values" approach was rejected despite providing a greater environmental protection standard. [170] Even if the domestic regime came into force after the investors' initial investment, they were still bound by it.[171] Regulations aided in establishing where impacts became significant and thereby constituted harm.

The Constitution remained relevant to the dispute. The Tribunal held:[172]

> "…that Constitution's focus on environmental protection means that when choosing between certain disputed (but reasonable) interpretations of the Ecuadorian regulatory regime, the interpretation which most favours the protection of the environment is to be preferred".

166 *Burlington,* above n 6, at [219].
167 At [219].
168 *Perenco,* above n 3, at [320].
169 At [321].
170 At [321].
171 *Burlington,* above n 6, at [1075].
172 *Perenco,* above n 3, at [322].

This was reflected in practice in relation to the applicable fault-based standard of proof. The Tribunal considered that "regulatory exceedances were indicative of operational failures and therefore should be taken as falling below the standard of care."[173] In this way, the applicable standard of liability was closer to the post-2008 strict liability scheme.

The tribunals also sided with the investors on the second issue. It held that the strict liability scheme established by the 2008 constitution did not have retrospective effect.[174] Any liability for harm alleged to have been caused by Perenco or Burlington prior to the entry into force of the Constitution had to be assessed in accordance with the prior fault-based regime.[175] Where Ecuador could demonstrate environmental harm post-2008 which was plausibly connected to the investment activities, the investors carried the burden of demonstrating that no such harm existed.[176]

Both tribunals made significant technical findings. The *Burlington* Tribunal identified correct guidelines for calculating impacted areas and volumes of impacted soils.[177] They also undertook their own site analysis to review the environmental impact the investors' activities had on mudpits, soil and groundwater.[178] The *Perenco* Tribunal is awaiting a final expert examination. This is an encouraging observation, especially given investment tribunals are primarily tasked with adjudicating commercial disputes.

The decisions are notable for the tribunals' willingness to acknowledge that Ecuador was entitled to seek compensation under domestic tort law.[179] It also upheld a states right to enforce a regulatory regime against investors to ensure compliance with its environmental obligations under international law. Both tribunals were confident to provide their own interpretation of Ecuador's constitution. This is especially so given it rejected many of Ecuador's submissions. The latter finding will be of interest to host states who wish to prioritise the protection of its environment. Broad standards contained in overarching constitutional documents may be overridden by narrower and lower standards contained in domestic laws and regulations. Overall, the Ecuadorian counterclaims are a welcomed development in the field of investment arbitration.

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173 At [374] and [379].

174 *Burlington*, above n 6, at [223]

175 At [234].

176 At [227].

177 At [372].

178 At [429] – [748].

179 Sundararajan, above n 1, at 25.

VI International Jurisprudence

Part VI surveys a range of international jurisprudence from the existing framework of international dispute resolution. While there is no strict doctrine of precedent in international investment arbitration, this exercise is useful in identifying the types of claims which have been inadmissible and the rationale behind this classification.[180]

This section will first examine the approach of the ICJ to the question of admissibility. Second, the treatment of counterclaims by the Iran-US Claims Tribunal will be explored. Third, how investment tribunals have interpreted counterclaim provisions will be critically assessed. Fourth and finally, a brief examination of the treatment of counterclaims and admissibility in international commercial arbitration and litigation will be considered.

In Part VII a summary of the main conclusions drawn from this exercise will be clearly articulated to formulate a new approach to admissibility.

A International Court of Justice

Since arbitrators have tended to avoid addressing issues of admissibility directly, one may seek additional guidance from the jurisprudence of the ICJ. General principles of law from ICJ jurisprudence can shape the arbitral process and where appropriate, may fill its gaps.[181] Arbitral tribunals have extensively referred to the decisions of the ICJ due to its perceived authority and persuasiveness.[182]

The ICJ is a useful point of comparison given its rule on counterclaims. Article 80 of the ICJ Rules of Court (the Rules), is very similar to art 46 of the ICSID Convention. The ICJ is permitted to "entertain a counterclaim only if it comes within the jurisdiction of the Court and is directly connected with the subject-matter of the claim of the other party".[183] The jurisdiction of the ICJ is also founded upon party consent.[184]

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180 Sarenmalm, above n 16, at 24.

181 Attila Tanzi and Filippo Fontanelli *The Law and Practice of International Courts and Tribunals* (Nijhoff International Investment Law Series, 2017) at 3.

182 Valentina Vadi *Analogies in International Investment Law and Arbitration* (Cambridge University Press, Cambridge, 2015) at 98.

183 ICJ Rules, art 80.

184 Musayev, above n 95, at 7.

It is unclear whether a connection in both fact and law is required for an admissible counterclaim.[185] A series of judges and commentators have argued that unless a connection of both fact and law is present, counterclaims have the potential to become a "formless cross-claim" with a scope far too wide.[186] This echoes the observations of Zimmerman and other's that invocation of an entirely new instrument in the counter-claim may be the basis for denying a sufficient connection.[187] Instead, the claim should be brought in a new case or explicit consent should be required from the principal claimant to permit the enlargement of the dispute.[188]

The ICJ in *Oil Platforms* found a middle ground and required a factual and legal connection, although the legal instrument did not have to be identical.[189] The Court exercised its jurisdiction to hear the United States' counterclaims despite Iran's argument that there could be no direct connection due to the vague and general nature of the claims.[190] The Court said that due to the lack of definition of "direct connection" in the Rules, the matter should be decided on a case-by-case basis.[191] The counterclaims satisfied the connectivity requirement as they "occurred at the same time and within the same area and pursued the same legal claim".[192]

A relationship between the time period and geographical location is usually present in admissible counterclaims. This was the case in *Land and Maritime Boundary* between Cameroon's claim that Nigeria had unlawfully occupied Cameroon's territory in the Bakassi Peninsula and with Nigeria's counterclaim that Cameroon had engaged in unlawful incursions into Nigerian territory along the same land border.[193] Similarly, in the *Bosnian Genocide* case, the Court rejected Bosnia's inadmissibility argument on the basis that the facts occurred within the same time frame (the 1990s) and geographical location (Bosnia and Herzegovina).[194]

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185 Kolb, above n 129, at 665

186 At 663.

187 Zimmerman, Tomuschat, Oellers-Frahm and Tams, above n 130, at 1009.

188 Kolb, above n 129, at 665.

189 *Oil Platforms (Islamic Republic of Iran v. United States of America) (Counterclaim Order of 10 March 1998)* [1998] ICJ Rep 190 at [38].

190 Constantine Antonopoulos *Counterclaims before the International Court of Justice* (Springer Publishing, 2011) at 86.

191 *Oil Platforms,* above n 185, at [39].

192 At [37].

193 Zimmerman, Tomuschat, Oellers-Frahm and Tams, above n 130, at 1010.

194 *Application of the Convention on the Prevention and Punishment of the Crime of Genocide (Bosnia and Herzegovina v Serbia and Montenegro) (Order)* ICJ 17 December 1997 at 254.

In *Oil Platforms*, Judge Higgins criticised the ruling of the Court and noted on the legal connection requirement, that:[195]

> …it is not essential that the basis of jurisdiction in the claim and in the counterclaim be identical. It is sufficient that there is jurisdiction. (Indeed, were it otherwise, counter-claims in, for example, tort could never be brought, as they routinely are, to actions initiated in contract.)

Kolb observes that the parties' arguments must fall within a single underlying "corpus of law" or in such a relationship that one set of arguments is the necessary precondition for the Court to form such an appreciation of the opposing party's arguments.[196] It is widely accepted that the legal source does not need to be identical.[197] The ICJ has also not required counterclaims to "diminish, offset or neutralise" the principal claim.[198] Lack of this element is not fatal to a counterclaim.[199] This interpretation significantly broadens the scope of admissible counterclaims.

It is notable that the Court in *Oil Platforms* recognised any analysis should be a holistic one. Establishing a connection should not be about strictly demarcating between factual and legal. The avoidance of a precise criteria is beneficial to adequately cater for the range of factual and legal situations which may arise. *Oil Platforms* demonstrates the "relative liberalism" of the ICJ's approach to connectivity. By enlarging the scope of permissible facts, the Court is able to view the totality of the overall dispute.[200] This feature of modern procedural law and practice has been criticised as blurring the line between a counterclaim and principal claim.[201]

As it stands, questions of admissibility have been confined to questions connectivity under art 80.[202] Although, there is nothing in the way of a State wishing to bring other challenges

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195 *Oil Platforms (Islamic Republic of Iran v. United States of America) (Separate Opinion of Judge Higgins)* [1998] ICJ Rep 190 at 218.

196 Kolb, above n 129, at 672.

197 At 672.

198 *Armed Activities on the Territory of the Congo (Democratic Republic of the Congo v Uganda) (Order of 29 November 2001)* (2001) ICJ Rep 660 at 667.

199 At 679.

200 Kolb, above n 129, at 673.

201 At 667.

202 At 670.

to admissibility, so long as they are based on the subject-matter of the particular counterclaim.[203]

B Iran/United States Claims Tribunal

The Iran-US Claims Tribunal was established under the Algiers Accords to resolve the Iran-US relationship crisis. Article II(1) of the Algiers Accords permits jurisdiction over counterclaims "which arise out of the same contract, transaction or occurrence that constitutes the subject matter of the principal claim." The Tribunal's jurisprudence provides assistance in relation to host-state counterclaims based upon general domestic law rather than in contract.

The Iran-US Claims Tribunal has denied counterclaims by interpreting the Claims Settlement Declaration to exclude counterclaims that arise by operation of law rather than from breach of the contract or transaction that constitutes the basis for the principal claim.[204] This encompasses domestic law, including revenue, social security and may have the scope to include environmental law.[205] A counterclaim is admissible where the contract includes specific obligations, which do not exist in general law, for example provisions which outline the payment of royalties.[206]

In *Harris International Telecommunications, Inc v Iran*, the respondent brought a counterclaim regarding the non-payment of social security contributions and related fines. The tribunal decline to exercise jurisdiction:[207]

> [t]he Tribunal has no jurisdiction over counterclaims for social security premiums that are based on municipal laws rather than on the contract which forms the basis of the claims.
>
> The Contract does not provide for any obligation of the Claimant to pay social security premiums in Iran. Any such obligation can therefore only stem from an application of Iranian law, which is also the legal basis on which the Respondent itself bases this

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203 At 670.

204 Charles Brower, and Jason Brueschke *The Iran–United States Claims Tribunal* (Nijhoff, The Hague, 1998) at 100.

205 David Caron, Lee Caplan and Marri Pellonpaa *The UNCITRAL Arbitration Rules: A Commentary* (Oxford University Press, New York, 2006) at 415.

206 At 415.

207 *Harris International Telecommunications, Inc. v Iran (Partial Award)* (1987) 17 Iran–U.S. CTR 31 at [176].

> Counterclaim. Thus, the Counterclaim for social security premiums and related penalties must be dismissed.

Similarly the Tribunal in *Computer Sciences Corporation v The Government of Iran* refused to exercise its jurisdiction over a claim involving the enforcement of Iranian tax law. The Tribunal distinguished between contractual and non-contractual claims, where the latter are inadmissible.[208] It observed that tax obligations stemmed from Iranian domestic law, as opposed to contract and therefore the Tribunal had no jurisdiction over the claim.[209] It also recognised:[210]

> …revenue laws are typically enormously complex, so much so that their enforcement is frequently assigned to specialized courts or administrative agencies. For these reasons, actions to enforce tax laws are universally limited to their domestic forum.

John Crook identified the proposition articulated in *Computer Sciences Corporation* as being a general principle of law applied in individual cases.[211] He states: "tax liabilities are created by the public law of a state and cannot be extraterritorially enforced."[212] Despite, this observation being made over two decades ago, it suggests that the inadmissibility of tax and social security claims can be attributed to something beyond the fact the obligation is not specified in a contract. It lends to something specific about the nature of tax and social security claims, such as both being inherently complex public law matters.

In several cases, the Iran-US Tribunal indicated that some claims could not be admissible as they raised political and non-justiciable questions.[213] The tribunal observed that to decide these claims would in effect require it to substitute its judgment for that of governmental agencies or officials.[214]

The jurisprudence from the Iran-US Claims Tribunal on the matter of admissibility of counterclaims is relatively clear. A legal symmetry of the counterclaim and principal claim must be present. Whether the rationale behind excluding claims which have their roots in

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208 *Computer Sciences Corporation v The Government of Iran* (1987) 10 Iran-U.S. CTR 269 at 312.

209 At 287.

210 At 312.

211 John Crook "Applicable Law in International Arbitration: The Iran-U.S. Claims Tribunal Experience" (1989) 83 The American Journal of International Law 278 at 298.

212 At 298.

213 George Aldrich *The Jurisprudence of the Iran-United States Claims Tribunal* (Oxford University Press, Oxford, 1996), at 130.

214 At.130.

domestic law can be equally applied to investment arbitration in the context of environmental claims will be explored further below.

C Investment Arbitration: ICSID/UNCITRAL Tribunals

Investment tribunals have grappled with the connectivity requirement. Scholars and tribunals have disagreed about the type of connection required between a host State's counterclaim and an investor's principal claim.[215] Where both claims arise out of the same contract, establishing the connectivity requirement is unproblematic. However, issues arise when the investor's claim concerns a treaty violation. Where both a legal and factual nexus is required, a claim based on the contract or domestic law would always be inadmissible since it would be based upon a different legal instrument.[216]

The Tribunal in *Saluka v Czech Republic* insisted upon the "interdependence and essential unity of instruments on which the original claim and counter claim are based".[217] As a result, the tribunal rejected jurisdiction over the counterclaim which was based upon Czech Republic's national law. This approach attracted considerable criticism and has since been departed from.[218]

In *Burlington*, the tribunal did not inquire into whether the counterclaim was based on the same legal instrument, suggesting that only a factual nexus is required.[219] The tribunal accepted jurisdiction over Ecuador's environmental counterclaim based upon national law.[220] A similar approach was taken in *Urbaser* which held there was a sufficient factual connection between the principal claim and Argentina's counterclaim. The investor's principal claim was related to the revocation of a contract to build infrastructure to provide water and remove contamination.[221] Argentina's counterclaim was based on violations of Argentine law and international law, including the right for access to water.[222] The Tribunal noted the claims were "based upon the same investment… in relation to the same concession."[223] Interestingly, the *Urbaser* Tribunal noted that "the legal connection was

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215 Musayev, above n 95.
216 Kjos, above n 57, at 149.
217 *Saluka*, above n 137, at [78] – [79].
218 Lalive and Halonen, above n 88, at 150.
219 Smith, above n 96.
220 *Burlington*, above n 6, at [73].
221 *Urbaser*, above n 92, at [34] and [1156].
222 At [1128].
223 At [1151].

also established to the extent the counterclaim is not alleged as a matter based on domestic law only."[224] The right for access to water was "the very purpose of the investment" and was encompassed by the protection scheme of the BIT.[225] The Court said:

> It would be wholly inconsistent to rule on Claimants' claim in relation to their investment in one sense and to have a separate proceeding where compliance with the commitment for funding may be ruled upon in a different way. Reasonable administration of justice cannot tolerate such a potential inconsistent outcome.

The respective counterclaims in *Burlington* and *Urbaser* are distinguishable. In *Burlington*, Ecuador's counterclaim was entirely based upon Ecuadorian domestic law and environmental protection did not feature in the BIT. Environmental protection also was not "the very purpose of the investment".[226] If we apply the reasoning of the *Urbaser* tribunal to the Ecuadorian counterclaims, it is unlikely they would have been considered admissible. Tribunals enjoy significant flexibility to find a claim admissible where consolidation of the claim and counterclaim would better administer justice.

Why was the tribunal in *Burlington* and *Urbaser* happy to exercise its jurisdiction over the host State counterclaim, whereas the *Saluka* tribunal refused to do the same? Can these alternative approaches be differentiated by something other than the application of legal and/or factual connectivity? Is there something about the nature of these claims which led the *Saluka* tribunal to require a legal connection, but the *Burlington* tribunal to merely require a factual connection? Did the tribunals take the correct approach? In attempting to answer these questions Judge Oda's comment in the *Oil Platforms* case should be kept in mind:[227]

> We should not simply put what may have originally been somewhat distinct matters into one melting-pot without making a careful examination of the essential character of that claim.

This raises the possibility that perhaps the inquiry should focus on the "essential character of the claim" as opposed to a connection. The connectivity requirement in itself has not been universally accepted as a prerequisite. The UNCITRAL Rules 2010 no longer require

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224 At [1151].

225 At [1151].

226 At [1151].

227 *Oil Platforms (Islamic Republic of Iran v. United States of America) (Separate Opinion of Judge Oda)* [1998] ICJ Rep 190 at 218.

connectivity. National and international practice suggests that juridical connectivity ought to be considered as a factor, but should not determine whether a tribunal exercises its jurisdiction or not.[228] A legal connectivity requirement was not recognised by Douglas in his Rule 26:[229]

> In accordance with the terms of the contracting state parties' consent to arbitration in the investment treaty, the tribunal's jurisdiction ratione materiae may extend to counterclaims by the host contacting state party founded upon a contractual obligation, a tort, unjust enrichment, or a public act of the host contracting state party, in respect of matters directly related to the investment.

Douglas' wide formulation of the character of an admissible claim cannot be taken at face value. If counterclaims are accepted purely on the factual basis that they relate to the investment, has the net not been cast too wide? Theoretically, Douglas' Rule 26 could capture obligations founded in a host States criminal law which would not be desirable.

Saluka, Paushok v Mongolia and *Amco Asia v Indonesia* demonstrate the limits of Douglas' Rule 26. The tribunals have refused to exercise jurisdiction for reasons which appear to be associated with the core character of the counterclaims themselves, rather than lack of legal connection. A counterclaim will almost always be inadmissible when the principal claim is based upon an IIA and a legal connection is required. This is because the host State's counterclaim will very rarely be based upon the same instrument. This frustrates a broadly formulated consent to arbitration which is found in most IIAs – "all disputes"- and cannot have been intended. As a result, alternative factors must be at play.

In *Saluka,* the Czech Republic brought counterclaims for various breaches of Czech banking, competition and tax laws. The Tribunal in *Saluka* observed that the legal basis of the counterclaim:[230]

> …is to be found in the application of Czech law, and involves rights and obligations which are applicable, as a matter of the general law of the Czech Republic, to persons subject to the Czech Republic's jurisdiction. Consequently, the disputes underlying those heads of counterclaim in principle fall to be decided through the appropriate procedures of Czech law and not through the particular investment protection procedures of the Treaty.

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228 Kjos, above n 57, at 150.

229 Douglas, above n 90, at 225.

230 *Saluka*, above n 137, [82].

The Tribunal in *Paushok* followed the approach in *Saluka* by linking the connectivity requirement with the domestic law of the host State.[231] The respondent brought seven counterclaims, among which included: alleging the claimant breached (1) tax, (2) fees and (3) levy obligations, (4) violated their licence agreements to extract gold efficiently and effectively, (5) violated environmental restoration obligations and (6) owed damages for gold smuggling.[232]

As for counterclaims 1, 2 and 3, the Tribunal refused to exercise its jurisdiction and found:[233]

> All these issues squarely fall within the scope of the exclusive jurisdiction of Mongolian courts, and are governed by Mongolian public law, and cannot be considered as constituting an indivisible part of the Claimant's claims based on the BIT and international law.

According to the tribunal, a decision on the merits in favour of Mongolia's counterclaims, would have the: [234]

> …likely effect of advancing the enforcement of Mongolian tax laws by non-Mongolian courts in respect of non-Mongolian nationals beyond limitations on the extraterritorial application of Mongolian tax laws rooted in public international law.

In addition:[235]

> …the generally accepted principle is the non-extraterritorial enforceability of national public laws and, specifically, of national tax laws.

Counterclaims 4, 5 and 6 were "found to relate to subjects being the object of Mongolian legislation and regulations; and moreover, the tribunal held they "cannot be seen as having a "close connection with the primary claim to which they are a response."[236] The Tribunal's

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231 *Sergei Paushok, CJSC Golden East Company and CJSC Vostokneftegaz Company v The Government of Mongolia (Award on Jurisdiction and Liability)* Marc Lalonde, Horacio A. Grigera Naón, Brigitte Stern 28 April 2011 at [693].

232 At [678].

233 At [694].

234 At [695]; Kjos, above n 57, at 153.

235 At [695]; Kjos, above n 57, at 153.

236 At [695].

treatment of Mongolia's counterclaims suggests that those which are covered by domestic law will never be admissible.

The Tribunal in *Amco Asia* dealt with Indonesia's tax fraud counterclaim in a similar way and was heavily relied upon by the Tribunal in *Saluka*. As noted by the second ICSID Tribunal, the counterclaim on tax fraud arose out of the application of "general law" to "persons who are within the reach of the host State's jurisdiction" and not "directly out of [the] investment" as required by art 25(1) of the ICSID Convention.[237] Accordingly, the counterclaim was held to be beyond its *competence ratione materiae*.[238] The Tribunal held:[239]

> …tax claims may be within ICSID's jurisdiction and that claims in relation thereto would be available to both parties to an investment dispute.
>
> 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. For these reasons the Tribunal finds the claim of tax fraud beyond its *competence ratione materiae*.

The Tribunal in *Amco Asia* emphasised the importance of explicitly including the general obligation of law owed by the investor in the applicable investment contract. Where this is the case, tax counterclaims may be admissible. Antonopoulos also suggests that counterclaims concerning tax obligations owed by an investor may be admissible where the dispute arises directly out of the investment being expressly contracted for.[240] This position is inconsistent with the Iran-US approach, accepted by Aldrich.[241] The Iran-US approach is that despite a general law obligation being included in a contract, the source of the obligation is still in general law and is inadmissible.

The approach to admissibility by investment tribunals has been inconsistent. The requirement that a counterclaim be based upon an identical legal instrument to the principal claim seems unduly narrow. It ignores the reality that investor obligations are very rarely contained in an IIA. The more recent approaches of *Urbaser* and *Burlington*, which require

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237 *Amco Asia Corporation and others v Republic of Indonesia* (*Decision of Jurisdiction in Resubmitted Proceeding)* ICSID ARB/81/1, 10 May 1988 at [122]-[127]; Kjos, above n 57, at 152.

238 At [124].

239 At [124] and [126].

240 Antonopoulos, above n 196, at 32.

241 Aldrich, above n 213, at 130.

a factual connection to the principal claim or that the counterclaim arise out of the investment, set a more desirable standard.

D International Commercial Arbitration and Litigation

International commercial arbitration plays a central role in dispute resolution regarding international business.[242] Unless the institutional rules governing the dispute permit counterclaims, a counterclaim can only be raised if it falls within the scope of the arbitration agreement.[243]Article 5(5) of the International Chamber of Commerce (ICC) Arbitration Rules does not include specific requirements for the admissibility of counterclaims. There is no prerequisite concerning the tribunal's subject-matter jurisdiction nor any connectivity requirement.

International courts have provided useful jurisprudence on whether a non-contractual counterclaim is still arbitrable. It has been generally accepted that a party may not defeat an arbitration clause by casting its claims in tort, rather than in contract.[244] The Court in *Ford v Nylcare Health Plans of the Gulf Coast Inc* observed: "Basing arbitrability merely on the legal label attached to it would allow artful pleasing to dodge arbitration of a dispute otherwise 'arising out of or relating to' the underlying contract."[245] However, tort claims which do fall outside the arbitration clause cannot be submitted to arbitration.[246]

A recent French case provides valuable insight as to the nature of admissible claims. A French distributor argued that a tort claim under a mandatory provision of French law could only be brought before a French Court, despite the parties consent to ICC arbitration to settle "all disputes arising out of or in connection with the present contract".[247] This argument was rejected and the Court compelled the parties to submit its claim to arbitration. The appeal court noted that the claim presented a sufficient connection with the contract since it arose from the circumstances that surrounded the termination of the contract and

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242 Akira Saito "International Commercial Arbitration and international Commercial Courts: Towards a Competitive and Cooperative Relationship" (2016) 20 Hors Serie 33 at 35.

243 Vladimir Pavić "Counterclaim and Set-Off In International Commercial Arbitration" (2006) *Annals International Edition* 101 at 104.

244 Gary Born *International Commercial Arbitration: International and USA* (2nd ed, Kluwer Law International, 2001) at 322.

245 *Ford v Nylcare Health Plans of the Gulf Coast* 141 F 4d 243 (5th Cir 1998) at 250-251.

246 Born, above n 237, at 323.

247 "Court confirms application of standard ICC arbitration clause to tort claims" (16 September 2010) International Law Office <www.internationallawoffice.com> at 1.

from the consequences that resulted from it.[248] The public policy considerations attached to the dispute, as well as the provision being mandatory in French law, did not invalidate the parties' consent to arbitration.[249] This appears to be the generally accepted position, except in cases where the subject-matter makes the agreement void (family law and intellectual property disputes).[250] This case is a reminder that parties will be held to the dispute resolution mechanisms they agree to.

Russell on Arbitration suggest that not all disputes are admissible, despite connectivity:[251]

> As a matter of English law certain matters are reserved for the court alone and if a tribunal purports to deal with them the resulting award will be unenforceable. These include matters where the type of remedy required is not one which an arbitral tribunal is empowered to give.

The point was illustrated in *Bilourne v Ghand*. The Tribunal refused to exercise its jurisdiction over human rights violations resulting from the arbitrary detention of an investor. The Tribunal noted:[252]

> [t]he Government agreed to arbitrate only disputes 'in respect of the foreign investment.' Thus, other matters – however compelling the claim or wrongful the alleged act – are outside this Tribunal's jurisdiction.

Mustill and Boyd note:[253]

> English law has never arrived at a general theory for distinguishing those disputes which may be settled by arbitration from those which may not.

This corroborates the lack of attempt to identify the principles or characteristics of a claim which may or may not be admissible. Investment tribunals have greater scope to impose penalties than that of commercial arbitrators. They adjudicate disputes in an accessible

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248 At 1.

249 At 1.

250 At 1.

251 David Sutton and Judith Gill *Russell on Arbitration* (22nd ed, Sweet & Maxwell, London, 2002) at 28.

252 *Biloune and Marine Drive Compex Ltd v Ghana Investments Centre and the Government of Ghana (Award on Jurisdiction and Liability)* (1989) 95 ILR 194 at 203.

253 Lord Mustill and Stewart Boyd *The Law and Practice of Commercial Arbitration in England* (2nd ed, LexisNexis, 1989) at 149.

public forum, unlike commercial arbitration which usually occurs behind closed doors. Due to these differences, the rationale behind excluding particular disputes from the reach of arbitration may not apply equally.

Tribunals have not shied away from assessing environmental matters in the past. Prima facie, there is no reason to suggest that the nature of environmental claims should preclude a tribunal from exercising jurisdiction over them.

Article 8(3) of the Brussels I Regulation (Regulation) outlines that a person domiciled in an EU Member State may be sued:[254]

> (3) on a counter-claim arising from the same contract or facts on which the original claim was based, in the court in which the original claim is pending.

This is restrictive approach goes beyond a requirement of close connection.[255] Courts have encountered difficulties primarily where the counterclaim is not based upon the same contract but from a series of closely connected contracts.[256] It is notable that the language used in art 8(3) does not provide clear guidance about when a counterclaim may arise from the same facts. Article 28(3) of the Regulation defines the term "related actions" to be when "claims are so closely connected that it is expedient to hear and determine them together to avoid the risk of irreconcilable judgments." It is tempting to interpret art 8(3) in the same way.

VII A New Approach to Admissibility

An assessment of the admissibility of counterclaims purely with reference to factual and legal connectivity is misleading. This is not to suggest that courts and tribunals have erred in reaching outcomes based on admissibility. Rather, they have oversimplified the inquiry. Such an inquiry is pertinent during a time where purely commercial disputes are being replaced by a hybrid of commercial and non-commercial matters. International jurisprudence suggests other factors are at play when courts and tribunals decide to exercise their jurisdiction over counterclaims. This section is intended to provide a summary of the

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254 European Council Regulation No. 44/2001 on Jurisdiction and the Recognition of Enforcement of Judgements in Civil and Commercial Matters (signed, 22 December 2000, entered into force 1 March 2001), art 8(3). (Brussels I Regulation).

255 Ulrich Magnus and Peter Mankowski (eds) *European Commentaries on Private International Law: Brussels I Regulation* (European Law Publishers, 2007) at 264.

256 At 265.

main conclusions drawn from this exercise in an attempt to formulate a new approach to admissibility. It is worth reiterating the definition of admissibility. Admissibility is whether the case itself is defective – whether it is appropriate for the tribunal to hear it.

Any inquiry into the admissibility of a counterclaim should be approached on a case-by-case basis. This was approach was endorsed by the ICJ in *Oil Platforms*.[257] The lack of guidance provided by institutional rules and conventions offers considerable flexibility to tribunals. A holistic approach is necessary to appropriately decide which kinds of disputes should be admissible before an investment tribunal.

Investment tribunals should be reluctant to dismiss a claim for lack of admissibility once jurisdiction has been established. The tribunal in *SGS v Paraguay* makes the point that "having found jurisdiction, we would have to have very strong cause to decline to exercise it' and it would be 'incongruous' to find consent and therefore jurisdiction yet to dismiss the claim on admissibility grounds."[258] Six key observations, relevant to the admissibility inquiry, have been identified below.

First, an admissible counterclaim must have an identical temporal and geographical connection to the principal claim. Factual connectivity remains an important pre-requisite, especially since the ICSID Convention and prior investment tribunals have explicitly recognised such requirement. This prerequisite avoids placing "distinct matters into one melting-pot".[259] These kinds of counterclaims will enable a tribunal to achieve a view of the totality of the overall dispute. Furthermore, combining these claims will usually be necessary in the best interests of justice (the avoidance of inconsistent awards) and procedural economy.

Second, an admissible counterclaim does not need to be based on an identical legal instrument to that of the investor's principal claim. This narrow requirement, endorsed by the Iran-US Claims Tribunal, unreasonably restricts an investment tribunal's ability to exercise its jurisdiction over counterclaims. Treaty-based arbitration would be particularly problematic. Where an investor's principal claim is based on the IIA, it should not be fatal to a host State's counterclaim for it to be based upon the investment contract or domestic law. This is a reasonable interpretation given that investor obligations are not usually

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257 *Oil Platforms,* above n 185.

258 *SGS Societe Generale de Surveillance SA v Republic of Paraguay (Decision of Jurisdiction)* ICSID ARB/07/29, 12 February 2010, at [176].

259 *Oil Platforms (Separate Opinion of Judge Oda),* above n 223, at 218.

present in IIAs.[260] Only until recently have IIA's appreciated the reciprocity of this legal instrument.[261] The comment of Justice Higgin's in *Oil Platforms* supports this approach.[262]

Third, the centrality of the investor obligation to the investment is a pertinent consideration. Douglas recognised in Rule 26 that any counterclaim must be "directly related to the investment". In *Amco Asia*, the respondent's counterclaim was rejected as it did not arise "directly out of the investment".[263] This connection requirement is distinct from that of a legal or factual connection to the principal claim. In *Urbaser*, the investor allegedly violated the right to access to water. This right was "the very purpose of the investment". There was a clear relationship between Argentina's counterclaim and the investment. Where an obligation is entirely disconnected to the investment, making it admissible may risk burdening an investment tribunal with a task which should properly be assigned to a domestic court.

Fourth, a host State's counterclaim need not be based in the "same corpus of law" as the investor's principal claim.[264] To limit counterclaims to those in the same category as the principal claim, as suggested by Kolb on ICJ jurisprudence, will undermine an investment tribunal's dynamic function. It also ignores the complexity and variety of the kinds of disputes being brought before it. This interpretation would make the Ecuadorian counterclaims inadmissible as they were based upon environmental law as opposed to foreign investment protection. Investment tribunals do not operate in an exclusive legal regime. As a result, counterclaims should not be limited to the commercial aspects of the particular investment.[265]

Fifth, provided the counterclaim arises directly out of the investment, it is not fatal for it to be based on tort, constitutional or regulatory law. Unlike judges, arbitrators are not bound to apply a particular set of procedural rules (unless the parties so request) and consequently enjoy a comparatively greater degree of procedural flexibility in how they resolve a dispute.

Sixth, public policy matters should not prevent counterclaims from being admissible. Investment treaty arbitration, unlike international commercial arbitration does not only affect the interests of the parties to the dispute, but often a wide range of groups and

260 Smith, above n 96.
261 Beharry and Kuritzky, above n 27, at 389.
262 *Oil Platforms (Separate Opinion of Judge Higgins)*, above n 191, at 218.
263 *Amco Asia*, above n 232, at [126].
264 Kolb, above n 129, at 672.
265 Kryvoi, above n 26, at 229.

individuals.[266] Public policy matters may be a relevant consideration, but should be approached on a case-by-case basis.

These six conclusions provide a framework for analysing the admissibility of environmental disputes.

VIII The Admissibility of Environmental Claims

Tribunals are increasingly adjudicating investment disputes which are characterised by largely non-commercial features. *Perenco* and *Burlington* represent the first environmental counterclaims to be brought by a host State against an investor. They are welcomed developments in investment arbitration. The admissibility of environmental counterclaims brought by a host State provides an interesting case study. Assuming that there are no jurisdictional hurdles regarding consent, this section applies the six considerations identified above to assess the admissibility of environmental counterclaims.

A Legal Perspective

A host State must base their claim on a legal obligation owed by the investor.[267] The parties must mutually agree upon the law that determines the source of the investor's obligation. If parties do not agree on the applicable law, the tribunal can apply the law it sees fit.[268] The source of the environmental obligation may affect the question of admissibility.

1 IIAs and international law

Investors may owe environmental obligations contained in the applicable IIA. The scope and content of such protections vary from treaty to treaty, therefore a complete taxonomy of environmental provisions is impractical. To avoid unnecessary complexities, environmental protection can be incorporated into treaties in three broad, yet distinct ways. First, where environmental protection is an express objective in the preamble of treaty.[269]

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266 Eric De Branbandere *Investment Treaty Arbitration as Public International Law* (Cambridge University Press, New York, 2014) at 148.

267 Jorge Viñuales *Foreign Investment and the Environment in International Law* (Cambridge University Press, Cambridge, 2012) at 94.

268 United Nations Commission on International Trade Law "Arbitration Rules" (2011) UNCITRAL <www.unictral.org> art 35(3).

269 Beharry and Kuritzky, above n 27, at 389.

Second, a treaty may oblige an investor to comply with environmental domestic law.[270] Third, environmental obligations can be imposed directly upon investors by virtue of a treaty.[271] These obligations may be positive, such as undertaking an environmental impact assessment, or negative, such as refraining from polluting or contaminating.[272]

Environmental concerns are beginning to infiltrate traditional IIAs schemes.[273] In saying this, however, substantive environmental obligations are scarcely imposed upon investors.[274] An example of this minority is the Morocco-Nigeria BIT. This BIT requires investors to maintain an environmental management system and meet international certification standards.[275] Investors also must comply with environmental assessment screening procedures prior to the establishment of the investment and conduct social impact assessments of potential investments.[276] This BIT has been heralded as a significant contribution to the reciprocity of investment treaties.[277] A counterclaim that alleges breach of a similar treaty obligation will almost always be admissible: the investor's principal claim shares the same legal instrument. Additionally, if an arbitration clause allows it, a host State may also be able to claim directly against the investor.

The general lack of environmental obligations in existing IIAs creates difficulties in establishing connectivity. An investor's principal claim is likely to be founded upon the applicable treaty, whereas it is more likely that a counterclaim will be based on other sources of international law or domestic law.[278] Despite this, a counterclaim may still be admissible. It is not essential that its foundation mirrors that of the principal claim.

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270 At 389.

271 Gordon and Poal, above n 15, at 23.

272 At 24.

273 Rosalien Diepeveen, Yulia Levashova and Tineke Lambooy "Bridging the Gap between International Investment Law and the Environment" (2014) 30 Utrecht Journal of International and European Law 145 at 158.

274 Nathalie Bernasconi-Osterwalder, Aaron Cosbet, Lise Johnson and Damon Vis-Dunbar *Investment Treaties & Why They Matter to Sustainable Development: Questions and Answers* (International Institute for Sustainable Development, 2012) at 35.

275 Reciprocal Investment Promotion and Protection Agreement between the Government of the Kingdom of Morocco and the Government of the Federal Republic of Nigeria, Nigeria –Morocco (signed 3 December 2016). [Nigeria-Morocco BIT].

276 Article 27.

277 Tarcisio Gazzini "The 2016 Morocco-Nigeria BIT: An Important Contribution to the Reform of Investment Treaties" (26 September 2017) Investment Treaty News <www.iisd.org>

278 Smith, above n 96.

General principles of international law may also impose enforceable environmental obligations upon investors.[279] Despite the traditional belief that only States owe obligations in international law, some argue that investors that operate internationally no longer enjoy immunity from international rules.[280] Many environmental principles and norms are hard to characterise as legal obligations.[281] They mostly serve as guiding principles to be elaborated upon by incorporation into domestic legislation.[282] For example the 'polluter pays' principle cannot be properly defined without reference to the "procedural and institutional framework" within which the principle operates.[283] This is primarily an issue of the applicable law, although it may also effect the connectivity inquiry. For instance, where a host State's counterclaim is primarily based on domestic law, it may also have roots in international law or be included in an inoperative section of the IIA. This was alluded to in *Urbaser* in the context of human rights.[284]

The *Urbaser* Tribunal noted that "the legal connection was also established to the extent the counterclaim is not alleged as a matter based on domestic law only."[285] This appears to reference the fact that the international right of access to water was also encompassed in the protection scheme of the BIT. This suggests that despite the absence of substantive obligations in an IIA, express reference to applicable international norms or principles may legitimately be construed to be the same as the legal instrument. This will make their admissibility more likely. This is particularly relevant in the context of environmental counterclaims since IIAs often contain vague environmental objectives which do not impose substantive obligations upon investors, yet reference to them is still valued.

2 Contractual obligations

An investment contract between the host State and investor may include environmental obligations. This may be substantive obligations, that either oblige an investor to comply with the host State's domestic law, or similarly comply with international environmental

279 Kryvoi, above n 26, at 219.

280 *Urbaser*, above n 92, at [1195]; *Investor-State Dispute Settlement: Review of Developments in 2016*, above n 36, at 22.

281 Douglas, above n 18, at 440.

282 At 440.

283 Priscilla Schwartz "The Polluter Pays Principle" in Malgosia Fitzmaurice, David Ong and Panos Merkouris *Research Handbook on International Environmental Law* (Edward Elgar Publishing, Cheltenham, 2010) at 249; Mohamed Sweify "Investment-Environment Disputes: Challenges and Proposals" (2016) 14 De Paul Business and Commercial Law Journal 133 at 141.

284 *Urbaser*, above n 92, at [1128].

285 At [1151].

obligations. For example, a concession agreement between Liberia and ADA Commercial stipulated that "the investor is obliged to comply with international standards, regardless of their status in domestic law."[286] Establishing admissibility will be straightforward where both the principal claim and counterclaim are based upon the applicable contract as the legal instrument is identical.

A contractual counterclaim may still be admissible against a treaty-based claim. It must arise directly from the investment, or be temporally and geographically related to the principal claim. An environmental counterclaim will arise directly out of an investment where:

(a) The failure of the investor to perform its investment activities, contracted for, has caused the environmental harm;
(b) Environmental harm is a by-product of the investor performing its investment activities;
(c) The investor has failed to comply with environmental obligations, such as an environmental impact assessment, which served as a pre-condition for the investment activity; or
(d) The environmental harm has occurred within the same geographical location and temporal period as the investor's activity.

It is hard to imagine a situation where an environmental counterclaim alleging a breach of the investor's obligation will be wholly disconnected from investment itself.

3 Domestic law

Environmental obligations can also be found in domestic law.[287] Article 42(1) of the ICSID Convention allows a tribunal to rely on these sources. IIAs and investment contracts may also expressly confirm that investors are bound by particular domestic obligations. For example art 12 of the Model Text for the Indian BIT 2016 states that investors shall be subject to and comply with the law of the host State including law relating to the conservation of natural resources. Concern for international environmental sustainability is now reflected in the majority of domestic investment legislation. For example, art 13 of the Qatar Investment Law no. 13 / 2000 states that the foreign investor must preserve the

286 Douglas, above n 18, at 434.

287 Kate Parlett and Sara Ewad "Protection of the Environment in Investment Arbitration – A Double-Edged Sword" (22 August 2017) Kluwer Arbitration Blog <arbitrationblog.kluwerarbitration.com>

safety of the environment against pollution, abide by all laws, regulations and instructions relating to public health and security.[288] The admissibility of a counterclaim based upon this type of obligation will be determined on whether there is a temporal and geographical connection with the principal claim or whether it arises directly from the investment.

Environmental obligations may be contained in public, tort, regulatory or constitutional legal instruments. Where tort law provides stronger protections than a contractual obligation, the host State will likely elect to base its counterclaim upon domestic law.[289] Counterclaims often reflect this choice.[290] The issue of causation is associated with the merits of a claim and should be avoided when inquiring into admissibility. The tortious basis of a counterclaim should not preclude its admissibility before an investment tribunal. Counterclaims founded on tort were recognised as being admissible by Judge Higgins in *Oil Platforms*,[291] Douglas' Rule 26,[292] as well the tribunals in *Perenco* and *Burlington*.[293]

Similarly, a counterclaim is not excluded if it is based on a national constitution. The extent to which the environment is protected under such public instruments will differ from state to state. The Ecuadorian Constitution imposes strict liability for environmental harm and affords special rights to nature. This was directly applied by the tribunals in *Perenco* and *Burlington*. It was particularly interesting that the both tribunals disagreed with Ecuador's interpretation of the measure of environmental harm that justified strict liability to attach. The tribunals' reasoning demonstrates the importance of a neutral forum to eliminate any perceived or actual bias which may exist in a domestic judicial system. Furthermore, where a host State brings a counterclaim it is signifying "resolute adherence to neutral third-party adjudication."[294]

B Policy Perspective

Aside from connectivity issues, there may be alternative reasons against admitting environmental claims or counterclaims in investment arbitration. Domestic courts may be

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288 Qatar Law on Organization of Foreign Capital Investment in the Economic Activity (Law No. 13 / 2000), art 13.

289 Iversen, above n 2, at 1.

290 *Burlington*, above n 6; *Perenco*, above n 3.

291 *Oil Platforms (Separate Opinion of Judge Higgins)*, above n 191, at 218.

292 Douglas, above n 90, at 225.

293 *Burlington*, above n 6; *Perenco*, above n 3.

294 Laborde, above n 15, at 101.

more appropriate fora to hear such disputes. Environmental issues are often connected to various national interests, unique to each state.

Mitigating the adverse effects of pollution and environmentally harmful activities is expected of both host states and investors in pursuit of their development. The relationship between environmental concerns and public health is particularly critical here.[295] Environmental harm is a vast concept: it can include the depletion of natural resources, contribution to climate change, depletion of fish stocks, pollution and the transfer of waste across boundaries.[296] Many of the acts that cause these harms are perpetuated by economic entities, rather than the host State themselves. The impacts of environmental harm are felt beyond the parties; they implicate the rights held by individuals, classes and nationals of the host State."[297]

As environmental law is perceived as a matter of public interest,[298] it may be argued that the adjudication of such disputes should be exclusively reserved to national courts and state regulation.[299] There are two reasons for this. First, these kinds of disputes should be adjudicated in a public forum. Given the greater public access to investment arbitration awards, the transparency concerns associated with commercial arbitration are not as applicable here.[300] Second, a host State should be seen as having exclusive control over foreign activities that occur within its territory, particularly when public policy is involved.[301] Dagbanji argues that the jurisdiction of domestic courts over issues such as human rights and the environment should be treated as "peremptory norms" which states cannot contract out of or impair by the agreements they reach with investors.[302] This argument is premised on the proposition that investment tribunals are ill-equipped to consider the protection of social and community interests, while simultaneously protecting foreign investors.[303] Previously, the absolute protection of foreign investments had usually,

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295 Nasser Mehsin Al-Adba "The Limitation of State Sovereignty in Hosting Foreign Investments And The Role of Investor-State Arbitration to Rebalance The Investment Relationship" (Doctorate Thesis in Law, University of Manchester, 2014) at 61.

296 Nollkaemper, above n 52, at 180.

297 Amado, Kern and Rodriguex, above n 60, at 55.

298 Nitish Monebhurrun "Is investment arbitration an appropriate venue for environmental issues? A Latin American perspective" (2013) 10 Brazilian Journal of International Law 195 at 200.

299 Elisa Morgera *Corporate Accountability in International Environmental Law* (Oxford University Press, New York, 2009) at 30.

300 De Branbandere, above n 266, at Y.

301 Dominic Dagbanja "Constitutionalism and local remedies rule as limitations on investor-state arbitration: perspectives from Ghana" (2017) 17 OUCJL 110 at 139.

302 At 134.

303 At 139.

if not always, been at the expense of communal interests.[304] There is a risk that societal well-being may be jeopardized in a large arbitration concerning environmental protection.[305]

Domestic adjudication of environmental disputes can have inherent conflicts of interest. Investment arbitration is a neutral dispute resolution forum, therefore is an attractive solution: it mitigates the risk of a compromised decision.[306] Host states have economic interests in the outcome of an environmental dispute, particularly for developing countries whose economic development is heavily dependent upon foreign investment.[307] Furthermore, host states may be considered as partially responsible for the damage, since they authorised the investors' activities.[308] Domestic courts may not have the capacity to adequately protect broader environmental concerns and the rights of those directly impacted by disputed harmful activities.

Environmental obligations typically involve a high level of "fudge".[309] The obligations upon investors are likely to be vague or incomplete.[310] Environmental law protections remain unsettled on the international stage.[311] Recourse to an investment tribunal, rather than a domestic court, might lead to inconsistent interpretations of domestic environmental regulations and standards. This was a concern of the International Atomic Energy Agency Standing Committee when deciding whether or not to establish a separate tribunal.[312] This is primarily due to the lack of a precedent system in investment arbitration. While inconsistency is a legitimate concern in the interpretation of domestic law, the concern has lower standing in international law. Investment arbitration may foster a common appreciation and interpretation of environmental norms and obligations. This could be valuable to both developed and developing host states, who are likely to have differing priorities when it comes to environmental protection.[313]

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304 Monebhurrun, above n 298, at 200.

305 William Park *Arbitration of International Business Disputes: Studies in Law and Practice* (2nd ed, Oxford University Press, New York 2012) at 697.

306 Slater, above n 13, at 136.

307 Morgera, above n 29, at 28.

308 At 28.

309 Sands, above n 47, at 67.

310 Beharry and Kuritzky, above n 27, at 389.

311 Sands, above n 47, at 67.

312 Sands, above n 54, at 910.

313 Sands, above n 47, at 67.

Environmental claims are rarely raised in isolation.[314] Investment tribunals are regularly tasked with the application of a cluster of rules.[315] This can be seen in the greater acceptability of investment tribunal's ability to hear disputes concerning revenue law, competition law, corruption and bribery, illegality and consumer law.[316] Tribunals should not avoid engaging with the wider framework within which investment relationships take place.

In some ways, environmental protection regulations can be said to have an administrative character. These kinds of regulations include obtaining licenses or permits for implementing activities – as well as the sanctioning of the behaviour that does not comply with the regulations or causes environmental damage.[317] When a state brings a counterclaim based on a domestic regulation, it usually exercises a right that private parties do not possess.[318] They are public and regulatory in nature.[319]

Environmental disputes are often highly complex. Identifying the scope of 'environmental harm' and the level that will attach liability to actions is regularly a contentious issue.[320] Evidence brought by each party is often dominated by competing scientific claims, as in *Perenco*. It is a misconception to say investment tribunals are not equipped to adjudicate these kinds of complex non-investment related matters. The Tribunal's approach in *Burlington* reflects this. The Tribunal demonstrated extensive engagement with the technicalities of identifying environmental harms, and made commendable efforts to accustom themselves with the practicalities of this complex area of law through site visits.[321] Jorge Viñuales praised the Tribunal for resorting to specific environmental techniques "without anything but the right amount of justification".[322] He concluded that environmental considerations seem "a normal, and even obvious, component of the

314 Valentina Vadi *Public Health in International Investment Law and Arbitration* (Routledge, 2012) at 135.

315 Asteriti, above n 24, at 272.

316 Emmanuel Gaillard and John Savage (eds) *Fouchard, Gaillard, Goldman on International Commercial Arbitration* (Kluwer Law International, The Hague, 1999), at [572].

317 Carmen Garcia-Castrillon "International Litigation Trends in Environmental Liability: A European Union-United States Comparative Perspective" (2011) 7 Journal of Private International Law 3 at 553.

318 Campbell McLachlan *Foreign Relations Law* (Cambridge University Press, 2014) at 447.

319 Amado, Kern and Rodriguex, above n 60, at 55.

320 Sands, above n 54, at 876.

321 *Perenco,* above n 3, at [429] – [748].

322 Jorge Viñuales "Foreign Investment and the Environment in International Law: The Current State of Play" (2015) in Kate Miles *Research Handbook on Environmental and Investment Law* (Edward Elgar, Cheltenham, 2016) at 34.

reasoning".[323] Investment tribunals have not shied away from enforcing environmental law against states.[324] No reasons exist as to why this should be any different in the context of counterclaims.

Arbitration enables parties to the dispute to nominate environmental law experts as arbitrators.[325] Similarly, an arbitrator with regulatory experience will be able to assess environmental regulatory standards. This was a key area of contention in the *Burlington* dispute. Specialised arbitrators provide a valuable perspective: they can assess evidence from practical and legalistic approaches. [326] This is especially important where the quantum of damages depends upon an expert's examination.

Despite engaging broader public policy issues, environmental disputes should still be admissible before an investment tribunal. Investment arbitration has proven to be a dynamic forum, capable of adjusting to the complex and a unique techniques required of environmental dispute resolution. The *Perenco* and *Burlington* decisions demonstrate the appropriateness and desirability of investment arbitration in this context. Where a host State's environmental counterclaim is temporally and geographically tied to the principal claim or where it directly arises from the investment, there is no reason that it should not be admissible. A more flexible approach to admissibility will increase the appeal and success of environmental counterclaims in the future.

C Arbitration as the Way Forward

A new approach to the question of admissibility will present investment arbitration as a feasible and appropriate forum for host states to pursue environmental claims against investors. To avoid admissibility hurdles, there are three particular steps host states should consider.

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323 At 34.

324 *Metaclad Corporation*, above n 14; *Tecmed*, above n 14; *Methanex*, above n 14; *S. D. Myers*, above n 14.

325 Benoit Le Bars *International Arbitration and the Protection of the Environment: Should the Existing Legal Instruments Evolve?* (UNCITRAL Papers for Congress, Modernizing Intenrational Trade Law to Support Innovation and Sustainable Development, July 2017) at 14.

326 Fraser Milner Casgrain "Arbitration of Environmental Disputes" (16 February 2012) Mondaq Business Briefing <www.mondaq.com>.

First, host states should modify their IIAs to ensure that environmental protection and economic development are equal priorities.[327] The inclusion of environmental obligation within an IIA preamble is a slack tool.[328] These obligations should be clearly drafted. Many IIAs have begun to move in this direction by explicitly including environmental investor obligations.[329] Where this is the case, the legal instrument of the principal and counterclaim may be identical, therefore determining admissibility is a facile task. Including specific provisions in IIAs that entrust tribunals with the ability to apply domestic law will make it easier for a tribunal to establish connectivity. In practice, renegotiation may be difficult especially for host states that wish to be seen as "investor-friendly".[330]

Second, the scope of the arbitration clause should be sufficiently wide to permit host states to bring counterclaims. This is an appropriate and necessary baseline in a properly drafted arbitration clause. Treaties which impose environmental obligations upon investors often explicitly exclude these kinds of disputes from arbitration.[331] The arbitration clause in *Urbaser* is exemplary as it expressly provides that a dispute could be submitted to arbitration at the request of either party. This kind of clause may permit host states to bring a direct claim for a treaty breach.

Third, host states should consider implementing "reverse umbrella clauses".[332] These clauses elevate a breach of domestic environmental law to the status of a treaty breach. Issues of connectedness will be removed. Furthermore, the application of domestic law may provide for a higher level of environmental protection than is contained in IIAs or general principles of national law.

IX Conclusion

This paper set out to examine the concept of admissibility and how investment tribunals should approach the inquiry in the context of environmental claims brought against investors. The paper has not attempted to provide a general overview of how environmental matters have arisen in such arbitrations. The focus has been on how environmental obligations can be used a sword by host states; in effect, reversing the classic paradigm of investor-state arbitration.

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327 Beharry and Kuritzky, above n 27, at 405.

328 At 384.

329 Asteriti, above n 24, at 272.

330 Beharry and Kuritzky, above n 27, at 409.

331 See for example Nigeria –Morocco BIT, art 27.

332 Laborde, above n 15, at 112.

The first part of this paper provided the contextual framework for discussion. It explained how the asymmetry of IIAs have led to a classic paradigm where host states have adopted the role of 'perpetual respondent'. Opportunities to enforce environmental obligations against investors are particularly uncommon given they are rarely included in IIAs and the narrow scope of arbitration clauses limiting the tribunals jurisdiction. As a result, the tribunals' approaches in *Perenco* and *Burlington* are novel.

With commentators routinely disagreeing on the distinction between jurisdiction and admissibility, it is no surprise that investment tribunals have had equally differentiated approaches. Many tribunals ignore the question of admissibility entirely. This was the case in *Perenco* and *Burlington*. This paper argues that the connectivity is inextricably part of the admissibility inquiry and should be examined separately to the issue of consent. Following a fine-grained analysis of international jurisprudence, this paper attempts to redefine the question of admissibility. It suggests that the inquiry should be approached on a case-by-case basis. Asking whether a counterclaim needs a factual and/or legal connection to the principal claim is oversimplifying the inquiry. So long as a counterclaim is temporally and geographically connected to the principal claim or arises directly out of the investment, it should be admissible. The traditional approach of requiring a legal connection is unreasonably narrow and ignores the multifaceted nature of contemporary disputes. The nature of a claim, including the extent to which public policy concerns are implicated, is another indication of whether a claim is admissible.

This paper has demonstrated that redefining the admissibility inquiry is valuable and integral to ensure that host state can pursue environmental claims against investors. For many host states, domestic tort law is most likely to provide the highest level of environmental protection. This kind of claim should not be precluded from adjudication for the reason it is not based upon the same legal instrument. Despite these kinds of claims being regulatory in character, as well as the consequences reaching individuals, this should not be a reason to exclusively reserve it to domestic court jurisdictions.

The tribunals in *Perenco* and *Burlington* engaged extensively with the complex technicalities associated with environmental claims. The reasoning is yet to attract academic criticism. Concerns about investment tribunals lacking the competency to deal with such claims are unfounded. Investment tribunals should have the ability to adjudicate disputes which transcend purely commercial matters. A holistic approach to the

admissibility requirement will facilitate this. Increased reciprocity will also increase investment arbitrations legitimacy as a dispute resolution forum.

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