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Jurisdictional Barriers to Bringing a Claim Based on Environmental Protection and Climate Change in Investment Arbitration

Krystal Lee and Teresa Queirós[1,2]

Abstract

Recent years have brought increased criticism of investment arbitration as a form of dispute settlement. In particular, several high-profile cases concerning renewable investments and environmental counterclaims have provoked much debate about the need for reform and/or alternatives to this method of dispute resolution.

However, although there have been increasing numbers of claims or counterclaims based on environmental protection or climate change in other fora, to date, this has not been met with much success in the context of investor-State dispute resolution.

This article considers that bringing these claims (or counterclaims) as part of investment treaty proceedings entails overcoming significant jurisdictional barriers. This article further considers the requirements needed to show the existence of a protected investment or a protected investor could act as a hurdle to potential investment claims based on environmental and climate change. This article also examines whether the requirement that a counterclaim be within the scope of the consent of the parties is becoming less of a hurdle than it was before.

I. Introduction

Recent years have seen increased criticism of investment arbitration ("**ISDS**") as a form of dispute settlement. The complaints about investment arbitration are wide-ranging and include, in particular, that the system fetters States' right to legislate in protection of the environment and the health of humans, plants and animals, and is an impediment to actions against climate change. Respondent States on the receiving end of arbitration notices have increasingly raised such legislation as a reason for modifying existing treaties providing for investment arbitration and, in some cases, walking away from the regime entirely.[3]

Notwithstanding the backlash, investment arbitration remains widely used as a means of dispute resolution between foreign investors and States given the existing treaties (and sunset clauses in treaties from which States have withdrawn). Consequently, given the increasing importance and publicity of environmental concerns, there has also been an uplift in claims

[1] Krystal Lee is dual-qualified in England and Wales (solicitor) and Paris and works at Dentons, specialising in international commercial and investment arbitration. Teresa Queirós is an English-qualified solicitor in LALIVE's arbitration practice group and focuses her practice on international arbitration.

[2] The views and opinions set forth herein are the personal views or opinions of the authors; they do not necessarily reflect views or opinions of the law firm with which they are associated.

[3] See, e.g., *UN investigates impact of investment treaties on human rights*, Kaminski, Isabella, The Lancet Planetary Health, Volume 7, Issue 10, e794 - e796 ("*States are increasingly moving towards terminating their existing stock of international investment agreements. They're doing that in part because of climate-related concerns, but also, more generally, because they think these treaties cut down their regulatory freedom*").

relate to environmental measures, protection and climate change being brought before investment tribunals, to varying degrees of success.

This article does not focus on the merits issues related to an environmental claim, including questions of causation, materiality and loss. Instead, Section II addresses the first step before such claims can even be advanced before a tribunal – the jurisdictional hurdles. It will first address the jurisdictional barriers for claimants seeking to advance environmental claims before an investment tribunal, in terms of the tribunal's subject matter and personal jurisdiction over these claims. It then briefly considers merits-based hurdles to bringing environmental claims. Section III will then consider instances when such claims are brought as a counterclaim by respondent States, including examples when such counterclaims have succeeded. Section IV considers the ways in which States can increase their chances of overcoming such jurisdictional barriers to claims and counterclaims to protect legitimate environmental and sustainable development objectives going forward. Section V summarises the conclusions reached.

II. Jurisdictional Barriers to Environmental Claims in Investment Arbitration

There is an increasing focus on climate change litigation before national courts (see, e.g., BIICL's corporate climate litigation platform) and before international courts such as the European Court of Human Rights (notably the *KlimaSeniorinnen v Switzerland* case). There is even a potential inter-State claim over alleged environmental damage.[4] Yet we have not seen many similar claims brought by claimants in an investor-State context, and none have been successful to date.

There are a number of reasons for this, including the fact that environmental standards are traditionally incorporated as part of national or international law and not an investment treaty, but there is a question of whether traditional jurisdictional requirements, and the concepts of what an investment is, and who qualifies as an investor, may act as a deterrent for these claims.

While investors have brought a large number of claims in the last 10-15 years arising out of changes to investment regimes applicable to renewables, this section of the article instead concerns environmental-based claims, namely claims brought by investors against a host State based on a failure to protect an aspect of the natural environment or based on failure to take action against climate change. This section concentrates on whether jurisdictional requirements are hurdles to investor-State disputes being brought to further environmental aims more directly (i.e. where the alleged treaty violation is closely related to a State's failure to protect the environment) and on the ways in which jurisdictional requirements could limit or prevent environmental claims, along with the sole example to the authors' knowledge where this was attempted.

[4] In January 2025 there were reports that the Philippines intends to lodge legal action against China over alleged environmental damage caused in the South China Sea. See for example, https://www.iareporter.com/articles/philippines-mulls-second-south-china-sea-claim-against-china-over-alleged-damage-to-maritime-environment/.

The classic jurisdictional hurdles [5] for ISDS claims are well-known to academics and practitioners. For the purposes of this article, we consider whether jurisdiction *ratione materiae* and *ratione personae* in particular can become hurdles for environmental claims.

Jurisdiction Ratione Materiae – A Question of Definitions

Arbitral tribunals must establish that there is a protected investment within the meaning of the relevant legal instrument in order to assume jurisdiction *ratione materiae*, and the question of whether a claimant has a valid investment is often raised by a respondent State. The question of what classifies as an investment may seem straightforward but is crucial to the success of a claim. In order to answer this question, parties and tribunals typically refer to what is stipulated in the relevant investment treaty and, in ICSID cases, may require satisfaction of additional jurisdictional conditions pursuant to Article 25(1) of the ICSID Convention. The latter famously provides that a dispute must arise directly out of an investment, without defining it,[6] which has led tribunals to grapple with the concept over the years.

The concept of investment is a curious one, in that it is one that may seem instinctively defined. One common theme is that it is linked to "capitalist" concepts of returns and profit – for example, the *MHS ad hoc* committee stated that "the 'ordinary meaning' of the term 'investment' is the commitment of money or other assets for the purpose of providing a return".[7]

Investment can be defined in a national law, an investment contract, or in a treaty.[8] It may be instructive to consider the definition of investment used in a recent investment treaty, such as that in the Comprehensive Economic and Trade Agreement entered into in 2017 between Canada and the European Union ("**CETA**"). This defines investment as:

> "**every kind of asset** that an investor owns or controls, directly or indirectly, that has the **characteristics of an investment, which includes a certain duration and other characteristics such as the commitment of capital or other resources, the expectation of gain or profit, or the assumption of risk**.
>
> […]
>
> Returns that are invested shall be treated as investments…" (emphasis added)

The definition of investment is a crucial ingredient to any climate or environment claims. Looking at the above definition from the perspective of a climate claimant, owning land to, for example, create a nature reserve, could qualify as an investment.

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[5] Namely jurisdiction materiae, personae and temporis.
[6] Article 25(1) of the ICSID Convention provides that "[t]he jurisdiction of the Centre shall extend to any legal dispute arising directly out of an investment".
[7] Dupuy, Pierre-Marie, About the Definition of an International Investment, in Jurisdiction in Investment Treaty Arbitration / gen. ed. Emmanuel Gaillard; ed. Yas Banifatemi ("**Dupuy**"), footnote 1 citing *Malaysian Historical Salvors, SDN, BHD v. Malaysia*, ICSID Case No. ARB/05/10, Decision on the Application for Annulment dated 16 April 2009.
[8] Kriebaum, Ursula, Dolzer, Rudolf, and Schreuer, Christoph, Principles of International Investment Law, 3rd Edition (2022; Oxford Academic) ("**Kriebaum, Dolzer and Schreuer**"), p. 86.

The above definition incorporates elements of the concept of investment developed by tribunals interpreting Article 25 of the ICSID Convention.[9] One of the most prominent of these decisions, *Salini v Morocco*, developed the so-called *Salini* test. This oft-cited formulation considered the four criteria for an investment, namely a substantial contribution, a certain duration of the operation, risk, and contribution to the host State's development.[10] While the first three criteria have been adopted widely, tribunals have been less willing to adopt the fourth criterion.[11]

Schreuer, commenting on Article 25, stated that "to identify certain features that are typical to most of the operations in question: the first such feature is that the projects have a certain *duration* [...] The second feature is a certain *regularity of profit and return* […] The third feature is the assumption of *risk* usually by both sides […] The fourth typical feature is that the commitment is *substantial* […] The fifth feature is the operation's significance for the host State's *development*".[12] Dupuy has noted that while this is similar to the *Salini* test, if an investment does not have one of these features this should not mean that a tribunal does not have jurisdiction, [13] and that the fourth *Salini* element "cannot, however, be accepted as an autonomous criterion for the identification of an investment unless expressly stated in the applicable BIT".[14]

So what does this mean for a claimant wishing to bring an environmental claim? One consideration is whether the investment is not being undertaken for profit. On one hand, why should whether an investment is being undertaken for profit matter if a claimant can show contribution, duration, and risk (leaving aside whether the investment contributes to the host State's development)? This raises interesting questions of whether an investment can be risky even if making monetary profit is not a goal. Instinctively, the answer would be yes – even if no profit is made, a claimant could potentially argue that there was a risk that the investment could be lost (even if there are no plans for it to grow in economic terms). In some ways, it appears that at least the CETA definition of investment could have a no return scenario in mind, as it provides that returns that are invested should also be treated as investments.

Interestingly, an economic definition of investment proposed in the past by Moselle could be read as incorporating a notion of value beyond pure economic value (e.g. profit), but could be read to include other values, such as greater environmental diversity. Moselle considered a macroeconomic and a microeconomic definition and finally proposed to definite investment as "the commitment by an individual or individuals of resources to any asset that will produce value in the future".[15]

One case to consider whether a not-for-profit investment could be an "investment" within a tribunal's jurisdiction *ratione materiae* is *Allard v. Barbados*. To the best of the authors' knowledge, this remains the only case to date in which a so-called environmental claim has proceeded to the merits.

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[9] *Ibid*, p. 88.
[10] *Salini Costruttori S.p.A. and Italstrade S.p.A. v. Kingdom of Morocco,* ICSID Case No. ARB/00/4, Decision on Jurisdiction, 16 July 2011, para. 52.
[11] Kriebaum, Dolzer and Schreuer, p. 92.
[12] Schreuer, Christoph H. The ICSID Convention: A Commentary, p. 128 (para 153), (Cambridge University Press, 2009) (emphasis in original).
[13] Dupuy, p. 44.
[14] Dupuy, p. 53.
[15] Moselle, Boaz, Economics and the Meaning of Investment, in Jurisdiction in Investment Treaty Arbitration / gen. ed. Emmanuel Gaillard; ed. Yas Banifatemi, p. 21.

In this case, Barbados raised a jurisdictional objection based on the fact that the claimant had not acquired an eco-tourism site in Barbados "in the expectation or use it for the purpose of economic benefit or other business purposes" such that the tribunal did not have jurisdiction over the investment.[16] Barbados based its arguments on the notion that the definition of investment require "an element of profit and purpose", and argued that "the Claimant has failed to establish that the Sanctuary project was established for anything other than for philanthropic or public benefit purposes related to the preservation of the environment, and most certainly not for the purpose of deriving an economic benefit to the requisite level of being directed to derive a commercial profit or for other business purposes".[17] It relied on an expert report by an accountant concerning concepts of commercial profit.

In contrast, the claimant argued *inter alia* that his business plans and financial projections contemplated at least a modest surplus, that he expected it would generate an economic return, and the Sanctuary was registered as and operated as a for-profit business.[18]

The relevant provision of the bilateral investment treaty ("**BIT**") between Barbados and Canada was Article 1 (f), which defines investment as "any kind of asset owned or controlled either directly or indirectly through an investor of a third State, by an investor of one Contracting Party in the territory of the other Contracting Party in accordance with the latter's laws…but does not mean real estate or other property, tangible or intangible, **not acquired in the expectation or used for the purpose of economic benefit or other business purposes**" (emphasis added).[19]

The *Allard* tribunal considered that the investment was acquired in the expectation and for the purpose of economic benefit. It found that "the preponderance of objective indicators shows clearly that [the claimant] was not creating a not-for-profit corporation".[20] The *Allard* tribunal's reference point for the claimant's expectations were his actual expectations and intentions at the time of acquiring the investment (and for that reason was not interested in the expert opinion provided by Barbados on the meaning and content of economic benefit).

In reaching its decision, the *Allard* tribunal noted that the corporate structures the claimant used to hold the investment were formed as for-profit corporations, the claimant was keen to limit tax exposure, the business plans contemplated an emerging surplus and "even repayment of capital advances, albeit with a low rate of return", while the claimant offered to transfer as a gift part of the lands involved him retaining the commercial and income generating parts (and this "presumably was intended to retain future income") and the claimant's "unchallenged statements in evidence that he had an expectation of getting his money back".[21] The tribunal came to this conclusion "[n]otwithstanding that the Tribunal might not be inclined to have formed the same expectations [as the claimant] as to future profit or repayment of investment", The tribunal found these expectations were honestly held by Mr Allard when establishing the Sanctuary and thereafter, "notwithstanding that during the Sanctuary's establishment and

[16] *Allard v Barbados*, PCA Case No. 2012-06, Award on Jurisdiction dated 13 June 2014 ("**Allard Jurisdiction Award**"), para. 27(2).
[17] *Ibid*, para. 36.
[18] *Ibid*, para. 37.
[19] Canada-Barbados BIT, cited in para. 26 of Allard Jurisdiction Award.
[20] Allard Jurisdiction Award, para. 45.
[21] *Ibid*, para. 50(6).

operations factors of profit were considered secondary and in the background to his principal motivations of environmental and public purposes".[22]

In light of this finding, the tribunal found it unnecessary to determine whether the Sanctuary was actually used for the purpose of economic benefit during its operations or the meaning of "other business purpose" "and whether such purpose requires profit-making over and above the making of revenues to allow operations to be self-sustaining". Curiously, the declaration by Professor Reisman appears to suggest that the tribunal was generous with respect to jurisdiction, but that this approach was correct because there was no indication the claimant was trying to mislead or defraud the government or gain an unlawful advantage.[23]

The tribunal's reasoning gives rise to some questions. Why should the corporate form of the investor (in this case a not-for-profit corporation) impinge on the question of whether there is a qualifying investment? What about cases of investment treaties (discussed in the next section) that specifically allow not-for-profit entities to be qualifying investors? More broadly, was the *Allard* tribunal correct to focus on the claimant's wish to minimise tax – and does the wish to minimise tax tell us anything about whether or not something qualifies as a protected investment? After all, one can imagine a charity with no aims to generate a return (let alone a profit) wishing to minimise its tax bill so that it can use more money for its charitable activities.

For a claimant, a solution may be to set up an entity as a for-profit entity, especially if this is for a project with environmental or other goals beyond generating a return. But should States consider more widely what making a profit is, and if it should take into account environmental concerns, rather than purely financial ones?

Jurisdiction Ratione Personae

The notion of whether a claimant is a protected investor is a similarly thorny path for those wishing to bring environmental claims. There does not appear to be a precedent for a decision considering whether a claimant fails to qualify as a protected investor because it was formed to further environmental goals (or any other not-for-profit goals). This may be a consequence of the fact that not all investment treaties will address this question, and so it is important to see what the requirements under the relevant investment treaty are.

Some investment treaties only extend protection to "for profit" entities. For example, while CETA's general definition of enterprise does not distinguish between for profit and not for profit entities,[24] the definition of investor includes a different definition of enterprise. In order for an enterprise to qualify as an investor and be able to invoke the protections of Chapter 8

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[22] *Ibid*, para. 51. Barbados attempted to resurrect this objection during the merits hearing, arguing that Mr Allard's answers under cross-examination only confirm that one of his motives for investing included environmental preservation, but the tribunal held that Mr Allard's elaborations as to his motivations "do not impugn the basis of the prior findings where the Claimant was successful where the Claimant was successful, if only just, on this issue of characterisation of his expenditures as an investment". (*Peter A. Allard v The Government of Barbados*, PCA Case No. 2012-06, Award dated 27 June 2016, para. 274. The tribunal in any event even if it were of the contrary opinion, considerations of issue estoppel or even *res judicata*, might have arisen. (*Ibid.*, para. 275).

[23] Declaration by Professor Reisman dated 27 June 2016 in *Peter A. Allard v The Government of Barbados*, PCA Case No. 2012-06.

[24] "[A]n entity constituted or organised under applicable law, **whether or not for profit**, and whether privately or governmentally owned or controlled, including a corporation, trust, partnership, sole proprietorship, joint venture or other association." CETA, Article 1.1 (emphasis added).

(Investment), it has to either have "substantial business activities in the territory of that Party" or be owned or controlled by an entity with substantial business activities.[25]

In contrast, in the more recently concluded BIT between Japan and Zambia, the definition of a protected corporate investor does not require that an entity be for profit.[26]

The CETA definition hints at what is commonly referred to as denial of benefits clauses, which is an issue that could affect an environmental claim. This is described as a method devised by States to "counteract strategies of investors that seek the protection of particular treaties by acquiring favourable nationalities" and while not all tribunals have considered this to be an issue of jurisdiction,[27] it is nevertheless instructive to consider it here.

If, whether as a result of the definition of investor or the application of a denial of benefits clause, a claimant may need to show "substantial business activities" which could be difficult for a charity or not for profit organisation to show. While the tribunal in *Pac Rim v. El Salvador*, considering the CAFTA provisions, contemplated whether the claimant holding company could have substantial activities (and in this case decided it could not).[28] The *Pac Rim* tribunal noted that the company in question had no employees, did not lease office space, did not have a bank account and its sole function was to hold assets. Based on this case alone, one could argue that as long as a company has a board of directors, board minutes, a continuous physical presence and a bank account that it would pass this test.[29] While it may seem counterintuitive to suggest that a claimant who is a not-for-profit entity, or involved in a not-for-economic profit business, may struggle to show it has "substantial business activities", based on this case alone, this may not be an insurmountable barrier.

In view of the above, while the terms of the relevant treaty will of course be key (including whether they associate either investment or investor with the making of profit or returns), claimants involved in not-for-profit investments would be wise to structure those investments carefully to overcome any jurisdictional or other hurdles.

Other Challenges of Bringing an Environmental ISDS Claim

Even if a claimant can meet all jurisdictional requirements to bring an environmental ISDS claim, such a claim will likely face broader challenges in the following stages of proceedings, particularly when it comes to questions of causation and evidence (both factual and expert).

First, it may be difficult to prove with certainty what caused the environmental degradation that is the subject of the claim, let alone prove a causal link between a State's conduct and the loss claimed, which would have consequences both for the merits and any damages aspect of the claim. A claimant may also find it difficult to establish when the event leading to injury took place, which could have implications in terms of whether the claim can even be brought,

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[25] Article 8.1, CETA.
[26] "The term "enterprise" means any legal person or any other entity duly constituted or organised under the applicable laws and regulations, whether or not for profit, and whether private or government owned or controlled, including any corporation, trust, partnership, sole proprietorship, joint venture, association, organisation or company" (Article 1(d)).
[27] Dolzer and Schreuer, p. 74.
[28] Pac Rim Cayman LLC v. Republic of El Salvador, ICSID Case No. ARB/09/12, Decisions on Jurisdiction or Preliminary Questions ("**Pac Rim**"), para. 4.68.
[29] Pac Rim, para. 4.72.

whether because it was brought outside a limitation period, or because it properly arose before the relevant investment treaty started to apply.

Second, when it comes to evidence, there may be more challenges. For example, claimants may face difficulties with evidence collection. While this may be an issue for claimants in ISDS cases generally, especially where claimants may have exited the investment or jurisdiction by the time proceedings take place, it may be particularly challenging when it comes to environmental cases given the nature of evidence that is required and the likelihood of multiple contributory reasons for any degradation of the environment.

Furthermore, access to evidence can be a significant impediment to a successful claim, particularly if the respondent State has exclusive access to or control over the necessary evidence. This is particularly the case given that tribunals may be cautious about reversing the burden of proof without the claimant proving at least some of its case. Document production in the course of proceedings may assist in this respect, but may not be sufficient for claimants to overcome this hurdle, given the potential for these documents, especially when it relates to policies and government decisions, to be covered by confidentiality obligations and/or applicable privilege concepts under local law.

As for expert evidence, both technical and quantum expert evidence are expected to be of assistance to a tribunal. With regards to technical expert evidence, this is likely to be a costly and extensive endeavour, given that the expertise required will probably be relatively niche and involve environmental scientists (as opposed to the more commonly seen cases of, e.g., construction or energy disputes, where the expert industry is highly developed and accessible). Furthermore, the relevant experts may also face a similar challenge as counsel in establishing with the required degree of certainty how the damage was caused and whether or not there is a causal link between it and the respondent State's conduct (or omission). This, in turn, has an impact on the quantum aspect of the case, which is usually the aspect of most concern for any claimant expending time and cost to bring the arbitration in the first place.

III. Jurisdictional Barriers to Environmental Counterclaims

As can be seen above, the barriers for claimants to bring a pure environmental claim before an investment tribunal are high. Respondent States sometimes raise environmental issues as a defence to claims, e.g., as a justification for particular legislative decisions taken to further public policy objectives such as the protection of the environment and/or human, plant and animal health. However, raising such issues as a counterclaim can also involve surmounting significant jurisdictional barriers.

As a preliminary point, States often choose to bring a claim against a foreign investor regarding a breach of environmental law, in a domestic court rather than in arbitration. This is because the relevant laws tend to be national laws for which the obvious forum is national courts. Furthermore, bringing the claim in national courts often enables the State to obtain immediate and mandatory relief where necessary, e.g., with injunctive relief against the investor from continuing certain activities that may exacerbate the environmental harm alleged to have been caused.

Nevertheless, there are occasions when respondent States in an investment arbitration may wish to bring a claim for breach of environmental law against the foreign investor within the arbitration instead of doing so in separate proceedings. This may be for a number of reasons.

First, doing so may allow the respondent State to reduce potential liability against a foreign investor for any alleged breach of international investment law pursuant to the relevant BIT (although, as explained below, a successful counterclaim, unlike a defence of set-off, is autonomous from the primary claim). Second, there may be procedural efficiencies to consider if the claims are dealt with within a single dispute resolution forum rather than in both arbitration and litigation.[30] Third, it may also result in a more advantageous enforcement position should the respondent State succeed, if the foreign investor's assets are held in jurisdictions that may otherwise be less favourable to enforcement of the respondent State's court judgment.[31] Finally, should a respondent State fail in its environment counterclaim in arbitration, depending on the circumstances of the case it could still bring the claim (or a variant thereof) before national courts instead, assuming it can overcome potential *res judicata* or issue estoppel arguments.

In this following section, previous cases of respondent States bringing such environment counterclaims in investment arbitration will first be considered, before some proposals as to how BITs could be redesigned to facilitate such claims.

Jurisdiction of Tribunals over Environmental Counterclaims

Counterclaims are expressly permitted under most major arbitration rules. Of most relevance to investment arbitration are the ICSID Convention and UNICTRAL Arbitration Rules.

Article 46 of the ICSID Convention provides that "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",[32] while Article 31(2) of the 2013 UNCITRAL Arbitration Rules state that "In its statement of defence, or at a later stage in the arbitral proceedings if the arbitral tribunal decides that the delay was justified under the circumstances, the respondent may make a counterclaim or rely on a claim for the purpose of a set-off provided that the arbitral tribunal has jurisdiction over it".[33]

Many other arbitration rules have broadly similar language. The key conditions for a respondent State to bring a counterclaim against a foreign investor, therefore, are (i) the counterclaim has a connection with the primary claim; and (ii) the counterclaim falls within the scope of consent of the parties. There is an additional requirement under the ICSID

[30] See, e.g., *Burlington Resources*, Decision on Counterclaims, p. 38 (para. 60) citing the agreement between Burlington et al. and Ecuador dated 26 May 2011, where Burlington consented to having the counterclaims arbitrated as the arbitration is the "appropriate forum for the final resolution of the Counterclaims arising out of the investments made by Burlington Resources and its affiliates in Blocks 7 and 21, so as to ensure maximum judicial economy and consistency" (emphasis added).

[31] The ICSID Convention provides for enforcement of ICSID awards in any Member State as if it were a final judgment of that Member State's courts: see Article 54(1). As for non-ICSID awards, the Convention on the Recognition and Enforcement of Foreign Arbitral Awards, to which 172 countries are parties, applies. Meanwhile, there is no equivalent system for the enforcement of foreign judgments; only a small number of States are party to the Hague Convention on the Recognition and Enforcement of Foreign Judgments in Civil or Commercial Matters: see Status Table.

[32] Article 46, ICSID Convention.

[33] Article 21(3), Revised (2010) UNCITRAL Arbitration Rules.

Convention for the counterclaim to fall within the scope of ICSID's jurisdiction within the meaning of Article 25 of the Convention.

Importantly, once a State is successful in bringing the counterclaim within a tribunal's jurisdiction, it becomes an independent claim that does not hinge upon the continued existence of the investor's original claim. Thus, a counterclaim may stand and continue to be decided upon by a tribunal even if the original claim were withdrawn or dismissed. Further, should the counterclaim succeed with a higher level of compensation awarded than the quantum of the investor's primary claim, that claimant investor becomes liable for the excess.

As indicated before, respondent States have infrequently filed for counterclaims in investment arbitration. Consequently, there have been few cases in which tribunals have agreed to exercise jurisdiction over a respondent State's environmental counterclaim, and fewer still where states have been successful in such counterclaims.

The most representative success cases are those against Ecuador in relation to the failed renegotiations of the terms of product-sharing contracts for Blocks 7 and 21 in the Ecuadorian Amazonian region following a spike in oil prices.[34] In both cases, Ecuador made counterclaims against the foreign investor, on the basis of the Ecuador-United States BIT in the case of *Burlington Resources v Ecuador* and the Ecuador-France BIT in the case of *Perenco v Ecuador*, *inter alia* for environmental damage found in Blocks 7 and 21 in the form of significant soil and groundwater pollution.[35]

Both were ICSID cases, meaning that Ecuador succeeded before both tribunals in demonstrating that (i) its environmental counterclaim was connected to the investor's claim; (ii) the foreign investor consented to having the counterclaim brought against them; and (iii) the counterclaim fell within the to the requirements of Article 25.

In *Burlington Resources v Ecuador*, the decision on jurisdiction was made easier by the fact that the claimant agreed not to raise an objection to the tribunal's jurisdiction over Ecuador's counterclaims, such that the second criteria on consent was unequivocally fulfilled.[36] Given that the counterclaims arose directly out of the subject matter of the dispute (i.e., Burlington's investment in Blocks 7 and 21) and also fulfilled the requirements of Article 25 (i.e. it was a legal dispute arising out of an investment and Burlington satisfied the requisite nationality requirement), the tribunal upheld jurisdiction over Ecuador's counterclaims (including its environmental counterclaim).[37]

In *Perenco v Ecuador*, the tribunal did not specifically rule it had jurisdiction on the counterclaims as this was not a question put to it by the parties. Instead, it ruled on a number of legal and factual issues in its Interim Decision on the Environmental Counterclaim, which it could not have done if it were not convinced that it had jurisdiction over Ecuador's

[34] *Burlington Resources Inc. v. Republic of Ecuador*, ICSID Case No. ARB/08/5 (formerly *Burlington Resources Inc. and others v. Republic of Ecuador*) and *Perenco Ecuador Ltd. v. Republic of Ecuador and Empresa Estatal Petróleos del Ecuador (Petroecuador)*, ICSID Case No. ARB/08/6.
[35] *Burlington Resources Inc. v. Republic of Ecuador*, ICSID Case No. ARB/08/5, Decision on Counterclaims dated 7 February 2017, p. 34 (para. 52).
[36] *Burlington Resources Inc. v. Republic of Ecuador*, ICSID Case No. ARB/08/5, Decision on Liability dated 14 December 2023, p. 39 *et seq*. (para. 93).
[37] *Burlington Resources Inc. v. Republic of Ecuador*, ICSID Case No. ARB/08/5, Decision on Counterclaims dated 7 February 2017, p. 39 (para. 62).

counterclaims.[38] Consequently, when Perenco later filed an Application for Dismissal of Ecuador's Counterclaims, the tribunal held that that Perenco had never "in the past challenged its jurisdiction to hear Ecuador's counterclaims nor their admissibility", such that when it did, it was deemed to be too late.[39]

It is notable that in both cases, the respondent State was able to overcome the hurdle of parties' consent to arbitration of the counterclaim either because the claimant voluntarily agreed to the tribunal's jurisdiction over those counterclaims (in the case of *Burlington Resources v Ecuador*) or made its objections too late in the proceedings (in the case of *Perenco v Ecuador*).

The decision in *Urbaser v Argentina*, in that respect, may provide further insight. The counterclaim raised by Argentina was also environmental in nature, specifically regarding the claimants' assumed investment obligations that Argentina argued gave rise to *bona fide* expectations that those investments would indeed be made and would make it possible to guarantee, in the area in question, the basic human right to water and sanitation.[40] In that case, the claimant contested (in a timely manner) the tribunal's jurisdiction over Argentina's counterclaim, arguing *inter alia* that the tribunal lacked competence to resolve the counterclaim (including because claimants' acceptance of the arbitration offer was delimited to the subject matter of their claim to the exclusion of other potential claims[41]) and that the counterclaim did not relate to a dispute arising directly from an investment within the meaning of the ICSID Convention and the BIT. The tribunal disagreed. It considered that the language of the relevant Argentina-Spain BIT provision (Article X) was broad enough to include circumstances where a State party may wish to sue an investor in relation to a dispute concerning an investment.[42] Further, in relation to the claimants' argument on consent, the tribunal considered that their acceptance (of the offer of arbitration) did not include any specific exclusion of potential counterclaims.[43] Having also satisfied itself that the counterclaims satisfied the other aforementioned conditions, the tribunal concluded that it had jurisdiction over Argentina's counterclaim.[44]

However, in this case, Argentina ultimately did not succeed on its counterclaim because, although the tribunal agreed that the right to water and sanitation to form part of human rights, it held that Argentina failed to prove that the claimants, as investors, were bound by an obligation *based on international law* to assure the local population's access to water and sanitation.[45]

While the above cases are examples of when respondent States successfully convince investment tribunals to exercise jurisdiction over their environmental counterclaims, tribunals

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[38] *Perenco Ecuador Ltd. v. Republic of Ecuador and Empresa Estatal Petróleos del Ecuador (Petroecuador)*, ICSID Case No. ARB/08/6, Decision on Perenco's Application for Dismissal of Ecuador's Counterclaims dated 18 August 2017, p. 20 (para. 43).
[39] *Ibid*, p. 18 (para. 35) and p. 20 (paras. 41-43) ("These issues [including all legal issues which "divided the Parties" with respect to Ecuador's counterclaims] have been determined by the Tribunal with finality" and the tribunal therefore "cannot now take a different view as far as the nature of its Interim Decision on the Environmental Counterclaims is concerned".)
[40] *Urbaser S.A. and Consorcio de Aguas Bilbao Bizkaia, Bilbao Biskaia Ur Partzuergoa v. The Argentine Republic*, ICSID Case No. ARB/07/26, Award dated 8 December 2016, p. 308 (para. 1156).
[41] *Ibid*, p. 299 (para. 1123).
[42] *Ibid*, p. 304 (para. 1143).
[43] *Ibid*, p. 305 (para. 1146).
[44] *Ibid*, p. 308 (para. 1155).
[45] *Ibid*, p. 320 (para. 1206).

are just as likely, if not more, to reject jurisdiction over such claims: see, by way of more recent example, *EEPL v Congo*.[46] In addition, because of the uncertainty of overcoming the jurisdictional barrier, respondent States may opt to use alternatives (i.e., domestic litigation) instead of bringing these counterclaims even when there are grounds to do so.

IV. Way Forward in the Development of Investment Agreements to Facilitate Environmental Claims and Counterclaims

As can be seen from the above, bringing environmental claims by way of claims or counterclaims in investment arbitration remains an unpopular strategy, both because of the relative advantages national court litigation presents, as well as the significant barriers in bringing such claims within an investment tribunal's jurisdiction.

Modern investment treaties have begun to reflect this challenge by expressly stating that States are entitled to regulate to achieve environmental protection. For example, CETA provides for the right of parties to "regulate within their territories to achieve legitimate policy objectives, such as the protection of the environment" and, it further provides that such regulation "does not amount to a breach of an obligation".[47] The Comprehensive and Progressive Agreement for Trans-Pacific Partnership similarly provides that "[n]othing in this Chapter shall be construed to prevent a Party from adopting, maintaining or enforcing any measure otherwise consistent with this Chapter that it considers appropriate to ensure that investment activity in its territory is undertaken in a manner sensitive to environmental, health or other regulatory objectives".[48]

Other treaties concluded in recent years have similarly taken a more proactive stance towards environmental protection. For example, the EU-Vietnam Free Trade Agreement has a chapter on trade and sustainable development, aimed at "promot[ing] sustainable development, notably by fostering the contribution of trade and investment related aspects of labour and environmental issues".[49] Similarly, the United States-Mexico-Canada Agreement ("USMCA") contains a chapter focused on *inter alia* promoting "mutually supportive trade and environmental policies and practices [and] high levels of environmental protection and effective enforcement of environmental laws".[50] However, it is noted that both treaties currently have limited ISDS provisions, if at all.[51] Thus, they may well be less significant on potential claims by foreign investors.

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[46] *EEPL Holdings v. Republic of Congo*, ICSID Case No. ARB/21/53. The decision remains unpublished, but a press release by EEPL dated 30 January 2024 indicates that the tribunal rejected jurisdiction over all of Congo's counterclaims, including one in relation to certain environmental remediation works at the Badondo site.

[47] CETA, Chapter 8 (Investment), Art. 8.9(1) and Art. 8.9(2) in relation to investment and regulatory measures.

[48] Comprehensive and Progressive Agreement for Trans-Pacific Partnership, Article 9.16 (Investment and Environmental, Health and other Regulatory Objectives).

[49] EU-Vietnam FTA, Chapter 13, Article 13.1.

[50] USMCA, Chapter 24, Article 24.2(2).

[51] During negotiations, the EU-Vietnam FTA was bifurcated into the current EU-Vietnam FTA and an EU-Vietnam Investment Protection Agreement ("IPA"), the latter of which contains dispute settlement provisions between foreign investors and Host States. The IPA has been approved by the European Parliament but has yet been ratified by Member States. As such, it has not yet come into force. As for the USMCA, the scope for "traditional" investor-state arbitration has also been much reduced as compared to its predecessor, the North American Free Trade Agreement. Canada is no longer a party to the ISDS chapter of the treaty, while there are also significant conditions and limitations to Mexico-US investment disputes (Chapter 14, Annex 14-D. See, in particular, Article 14.D.5).

One way to ensure that environmental claims can be brought in an ISDS context is for the definitions of investor and investment to foresee, or at the very least not foreclose, this possibility. For example, the definition of investor could expressly include not-for profit entities, and the definition of investment could allude to the fact that an investment does not need to be undertaken only or partly for profit for it to benefit from protection. With regard to investment, if a State wants to expand the definition to cover investments which benefit the environment but may not be done for profit, it could avoid referring to the Salini characteristics (which the SADC model BIT suggest States incorporate).[52] Alternatively, the definition of investment could require that in order to qualify as an investment that an asset must contribute or otherwise be significant to a Host State's development. For example:

> Investment means every kind of asset admitted or established in accordance with the laws and regulations of the Host State in whose territory the investment is made, that an investor owns or controls, directly or indirectly, whether or not for profit, and which contributes or is of significance to the Host State's development.

With regard to counterclaims, while changes to substantive provisions to reflect environmental concerns are an important development, they do not necessarily address the jurisdictional barriers faced by respondent States. For example, the amendments to the Energy Charter Treaty include provisions that reaffirm the respective rights and obligations of the Contracting Parties under multilateral environmental and labour agreements, such as the UNFCCC, the Paris Agreement and ILO fundamental conventions.[53] Nonetheless, they do not address the aforementioned jurisdictional obstacles and, thus, arguably still do not provide States with certainty as to being able to bring such environmental counterclaims against foreign investors.

One option for States may be to enter into (or negotiate an amendment to existing) investment agreements which expressly provide that, where a foreign investor initiates arbitration pursuant to the bilateral or multilateral investment agreement, they are deemed to have consented to the jurisdiction of the tribunal over potential counterclaims made by the State, subject to the applicable rules (i.e., that the counterclaim is connected to the primary claim and, in the case of ICSID arbitration, that the requirements pursuant to Article 25 of the Convention are satisfied). This will pre-empt the type of argument advanced by the claimants in *Urbaser v Argentina* in relation to the limits of their acceptance of the state's offer of arbitration and ensure that investors are unable to make a carve-out of potential counterclaims in their acceptance to arbitrate. By way of example, Article 19.2 of the 2022 South African Development Community Model BIT expressly provides that a host State "may initiate a counterclaim against the Investor before any tribunal established pursuant to this Agreement for damages or other relief resulting from an alleged breach of the Agreement". This may provide some degree of comfort to States as their ability to bring a counterclaim under the instrument, although the provision does not expressly indicate that a claimant bringing an investment arbitration under that agreement is deemed to have consented to the tribunal's jurisdiction over such a counterclaim.

Adoption of this approach will enable counterclaims, environmental or otherwise, to be brought without the barrier of parties' consent, to which claimants have little incentive to agree after the commencement of arbitration. Together with the developments already seen regarding substantive environmental protection provisions, this approach could permit respondent states

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[52] SADC Model Bilateral Investment Treaty Template with commentary dated July 2012.

[53] Energy Charter Treaty Conference decision **CCDEC202210** "Public Communication explaining the main changes contained in the agreement in principle", p. 6.

to have a viable opportunity to bring its environmental claims against errant foreign investors before an investment arbitration tribunal.

V. Conclusion

The need to prove that a tribunal has jurisdiction *ratione materiae* and *ratione personae* can act as a gatekeeper to potential investment claims based on environmental and climate change. While the terms of the relevant treaty will of course be key (including whether they associate either investment or investor with the making of profit or returns), claimants involved in not-for-profit investments would be wise to structure those investments carefully to overcome any jurisdictional hurdles or other hurdles such as the requirement to show substantial business activities. However, in a time increasingly concerned with environmental protection and climate change, should States consider vesting investment protections on investments that seek environmental aims, rather than purely financial ones?

Bringing environmental claims by way of counterclaims in investment arbitration remains an unpopular choice, but for different reasons. The relative advantages national court litigation presents cannot be underscored, together with the significant barriers in bringing such claims within an investment tribunal's jurisdiction. States can address this by including a provision in the relevant instrument expressly stating that if a foreign investor initiates arbitration under an investment agreement, they are deemed to have consented to the tribunal's jurisdiction over any counterclaims, subject to the applicable rules.

Either way, it is evident from the more recent bilateral and multilateral investment treaties that environmental issues are a key area of concern for States as they consider better ways to address them in international legal instruments. Examples include modifications to the Energy Charter Treaty and CETA. Undoubtedly, the ways in which investment tribunals may give these provisions teeth by overcoming the initial jurisdictional hurdles will continue to be explored by counsel for investors and States alike.