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An Unlikely Tandem of Criminal Investigations and Arbitral Proceedings: A Case Study of the INA – MOL Oil & Gas Proceedings

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Arbitral tribunals are increasingly faced with allegations of corruption. In these situations, arbitral proceedings and criminal investigations frequently go in tandem. Their findings overlap and may influence one another.

Regardless of the many instances where corruption is alleged, there have been only a few investment cases in which a finding of corruption was actually made.

Arbitral tribunals made findings of corruption in *World Duty Free v. Kenya* (2006) and *Metal-Tech v. Uzbekistan* (2013). In *World Duty Free*, the tribunal found that the payment of $2 million to set up duty-free airport stores constituted a bribe, invalidated the investment contract, and it denied the claimant any relief. In *Metal-Tech*, the tribunal found that the corrupt payment of $4 million in "consultancy" fees to the Prime Minister's brother placed the investment outside the BIT's protection.

In *Siemens v. Argentina and Niko Resources v. Bangladesh*, corruption was established on the basis of a positive finding by another authority. In *Niko*, Bangladesh presented a plea agreement between Niko and Canadian prosecutors, where Niko confessed to paying a bribe to the Bangladeshi Minister for Energy in 2005. Niko had not participated in any acts of corruption after 2005. Consequently, even though there was a finding of corruption, "there [wa]s no link of causation between [Niko's] established acts of corruption and the conclusion of the agreements", since the Bangladeshi minister who had taken bribes from Niko resigned quickly thereafter, before the signing of the relevant agreement.

The relationship between arbitral and criminal proceedings raises several interesting questions. Some of the recent Croatian arbitration cases, including the two arbitral proceedings involving INA Industrije Nafta d.d. (INA) and MOL Hungarian Oil and Gas PLC. (MOL), provide a good opportunity to analyze the impact of criminal investigations on arbitral proceedings.

INA – MOL Oil & Gas Arbitration Proceedings

INA is Croatia's most significant enterprise in the oil & gas field. In 2002, the Croatian Parliament

passed the INA Privatization Act to transform INA from a state-owned to a privatized company. In an open public tender, MOL won the tender with a bid of $505 million against OMV's offer of $420 million.

Between 2003 and 2011, MOL progressively built up its shareholding in INA, becoming the largest shareholder of the company with a 49.1% stake. The Government of Croatia is the second largest investor with 44.84%.

In 2009, MOL gained management control of INA through the First Amendment to the Shareholders Agreement (FASHA). In the same year, the parties negotiated one more crucial contract: the Gas Master Agreement (GMA; with FASHDA: 2009 Agreements), under which INA's gas storage and trading businesses were to be spun off into separate subsidiaries and transferred to the Government.

The circumstances in which the 2009 Agreements came about lie at the heart of the dispute. Croatia maintains that the 2009 Agreements were procured by MOL's Chairman Zsolt Herna?di's bribing of Croatia's then Prime Minister Ivo Sanader.

Two Parallel Arbitrations: UNCITRAL & ICSID

In November 2013, MOL initiated an ICSID arbitration against Croatia over violations of obligations concerning MOL's investments in Croatia (ICSID Case No. ARB/13/32). Claims are asserted under the Energy Charter Treaty for the unfair and inequitable treatment and expropriation of MOL's investments in Croatia.

In January 2014, Croatia responded to MOL by filing an UNCITRAL arbitration (PCA Case No. 2014-15) pursuant to the INA Shareholders Agreement and GMA, with the place of arbitration in Geneva, Switzerland. The Government requested that the 2009 Agreements be declared null and void, that MOL pay damages caused by its conduct, and account to Croatia for INA's conduct since January 2009.

In both arbitrations Croatia's main argument is that MOL procured the 2009 Agreements by corruption. To meet its burden of proof, Croatia relied on the Croatian Supreme Court's verdict against Sanader (November 2012), convicting Sanader for taking a €5m bribe from MOL in exchange for facilitating the 2009 Agreements.

However, in July 2015, Croatia's Constitutional Court annulled the corruption conviction on grounds of procedural errors and ordered a retrial, which started in September 2015.

While the ICSID arbitration is still pending, the outcome of the UNCITRAL arbitration became known to the Croatian public through an urgent press conference called by Croatian Prime Minister Andrej Plenkovi? on Christmas Eve.

Plenkovi? confirmed that the UNCITRAL tribunal has overruled Croatia's request to nullify the 2009 Agreements, finding that the evidence was not sufficient to prove corruption. The full award has not yet been made public.

MOL published excerpts from the award, where "rejecting all submissions and contentions to the contrary, the Arbitral Tribunal FINDS, DECLARES, RULES, ORDERS and AWARDS that Croatia's claims based on bribery, corporate governance and MOL's alleged breaches of the 2003

Shareholders Agreement are all dismissed."

With regard to bribery the tribunal found that:

> Having considered most carefully all of Croatia's evidence and submissions on the bribery issue, which has been presented in a most painstaking and comprehensive way, the Tribunal has come to the confident conclusion that Croatia has failed to establish that MOL did in fact bribe Dr Sanader. Accordingly, Croatia's case that the FASHA and GMA be rendered null and void due to the alleged bribery fails.

This is particularly important in light of the fact that during the UNCITRAL proceedings, at the invitation of the president of the arbitration, Sanader gave full testimony (with cross-examination). Sanader himself disclosed this fact in a 2014 interview with the Croatian media.

Criminal Investigations and Arbitral Proceedings: Three Questions

In the case of competing forums, the applicable law can have a significant impact on whether a positive finding of corruption is issued. Courts and tribunals may come to different conclusions concerning the same facts and legal issues. Consequently, there is a high risk of issuing conflicting decisions.

Moreover, arbitrators do not have the same resources or investigatory powers as criminal prosecution authorities. While a corruption finding may be the crucial issue of the case, arbitrators may not have the necessary tools to establish it.

In analyzing this tension, I briefly consider two questions, with special application to INA MOL arbitrations.

1. What is the Effect of a Criminal Court's Corruption Verdict on a Pending Arbitration?

Generally, a criminal verdict does not have a binding effect on the arbitral tribunal.
In *Inceysa Vallisoletana v. El Salvador*, the tribunal held that state parties' findings as to the legality of investment are not determinative. This is for the tribunal to determine, and domestic court findings are not *res judicata* for the purposes of determining jurisdiction.

Following this approach, in the UNCITRAL arbitration, MOL asserted that Croatia offered no support that the Sanader judgment "should be given automatic legal effect in an international arbitration." (Decision, ft. 5) MOL's position is that the Sanader judgment is of no relevance to the validity of the disputed agreements.

In the *Sanader decision*, the Croatian Constitutional Court expressly addressed this question and opined that domestic court decisions do not have *res judicata* effect in international arbitration proceedings:

> Decisions by national courts, including those by the Constitutional Court, cannot in general have an impact on arbitration proceedings initiated or conducted by the Republic of Croatia in the field of international commercial law. It is a general

> principle that arbitral tribunals are not bound by final judgments of national courts, or decisions issued by national constitutional courts, because such judgments and decisions are regarded as facts by arbitral tribunals. Such tribunals examine matters in the case before them on their own.

However, even if the criminal verdict has no binding effect, it will be taken into account in the arbitrators' assessment of evidence.

2. What is the Effect of a Criminal Court's Corruption Verdict on the Enforcement of an Award?

An award upholding a contract deemed by a criminal court to be tainted by corruption may be challenged at the enforcement stage on public policy grounds (Article V(2)(b) New York Convention). The likelihood of an award being set aside or denied enforcement on this ground will depend on the extent of the court's review powers and its understanding of what constitutes public policy.

In the Constitutional Court's decision quashing the *Sanader verdict*, the Court opined that contracts procured through corruption are per se contrary to state interests and public policy:

> The very fact that a person under the office of prime minister offers or accepts a bribe to influence the conclusion of a legal transaction within the competence of the Government – within the limits of his authority – makes the legal transaction concerned corruptive a priori in the substantive sense, … Each such transaction is *per definitionem* contrary to the interests of the Republic of Croatia.

Conclusion

The co-existence of parallel proceedings, such as in the INA MOL disputes, presents a number of risks for the parties. Different tribunals may reach different conclusions, and such conclusions may contradict domestic criminal law findings.

The uneven state of arbitration jurisprudence reflects the lack of consensus on how to deal with corruption in international disputes. Regardless of the proclaimed "zero tolerance policy" towards corruption, unforeseeable outcomes did little to deter litigants from bringing disputes involving corruption to the international arena.

This leaves us with several queries: Is the situation desirable where local verdicts finding corruption can be rejected by tribunals? In what way can the two be reconciled? Should there be a presumption that criminal judgments are *prima facie* valid? What if domestic proceedings are flawed?

It remains to be seen how the INA MOL claims, and in particular the issue of parallel criminal proceedings, will be approached by the ICSID tribunal. Croatian Prime Minister Plenkovi? announced that the ICSID award is expected in the summer of 2017.

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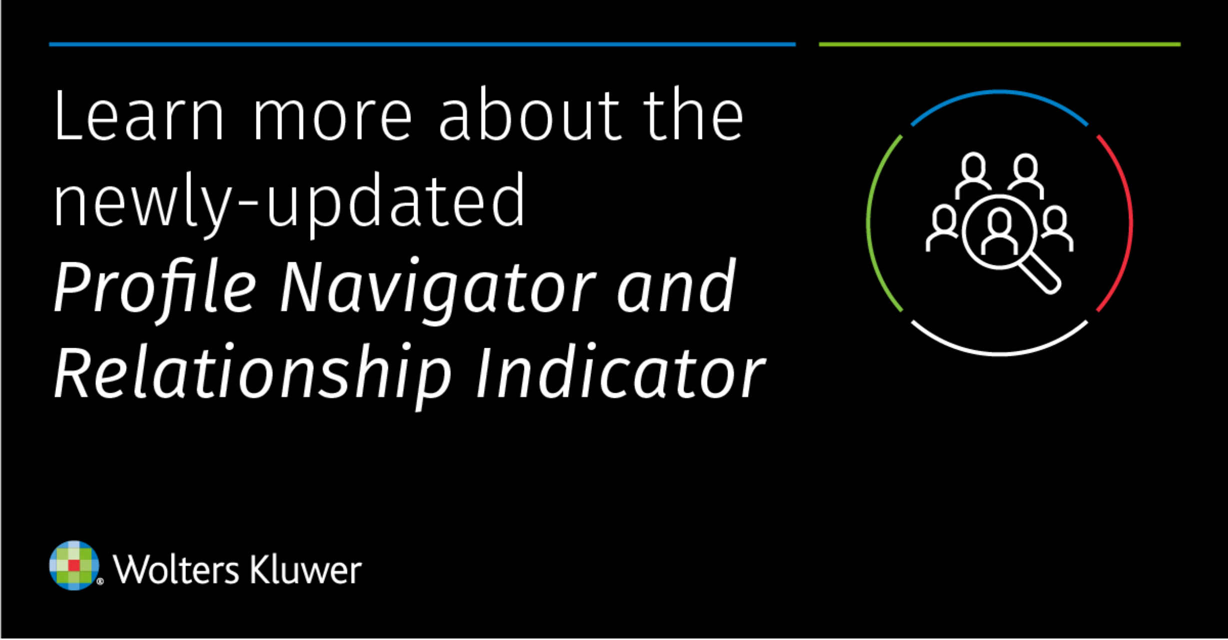

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