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MOL v. Croatia Saga: A Two-Faced Janus in the ISDS Reform Debate

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The current debate on the future of the Investor-State Dispute Settlement (ISDS) system seems not to leave anyone indifferent. Two camps can be discerned in the debate; the first comprising those who would argue that ISDS is in need of reform, and the second those who defend the ISDS system as is. The MOL v. Croatia saga, which has been dragging on since 2013, seems destined to further divide the debate, with its peculiarity lying in the opportunity for both camps to use the dispute to their advantage.

1. Factual Background

The origin of the dispute between MOL (a Hungarian multinational oil ang gas company) and Croatia can be traced back to 2008 when MOL managed to increase its shares in INA (Croatian multinational oil company) to 47.16 %. This was followed in 2009 by amendments to the Shareholder Agreement between the Government of Croatia and MOL. As per the amendments, MOL was given control over INA, and the Government agreed to take over INA's gas storage facilities and to take over the business of gas sales. The former Prime Minister of Croatia Ivo Sanader was subsequently arrested on allegations of bribery. When the amendments to the Shareholder Agreement were concluded, Sanader was still in office, and he allegedly accepted bribes from MOL in order to facilitate their conclusion.

In 2013, MOL initiated arbitration proceedings against Croatia before ICSID, claiming that Croatia's actions were in breach of the Energy Charter Treaty (ECT). Croatia responded in 2014 by initiating arbitration proceedings based on the Shareholder Agreement under the UNCITRAL Rules, arguing that, on account of the alleged corruption on the part of Sanader, the amendments to the Shareholder Agreement were null and void. The two arbitration proceedings were conducted in the shadow of the criminal trial of Sanader before the Croatian courts.

2. Croatian Criminal Trial of the Century

The lower court found Sanader guilty and sentenced him to 10 years in prison.[1] The Supreme Court of Croatia confirmed the verdict, but reduced the sentence to 8 years and 6 months in

prison.[2] The case then reached the Constitutional Court of Croatia which set aside the decision and ordered retrial, which culminated in a guilty verdict and a sentence of 6 years in prison. The Supreme Court then confirmed this verdict. In addition, the Croatian courts tried the CEO of MOL Zsolt Hernádi *in absentia*, finding him guilty of bribing Sander and sentencing him to 2 years in prison (the Hungarian authorities refused to extradite Hernádi).

While the trial was closely followed in Croatia by the media and the public at large, though largely did not become a divisive or politically-charged affair. That being said, two independent monitors of the trial –Judge Kai Ambos (Chair for Criminal Law at the University of Göttingen and Judge at the Kosovo Specialist Chambers in the Hague) and Lord David Anderson QC (British barrister and judge who was the Independent Reviewer of Terrorism Legislation in the United Kingdom) – wrote a Report in which they expressed concern that the prosecutors and the Croatian judiciary had exhibited bias in favour of Croatian national interests, and that, in the process, Article 6(1) of the European Convention of Human Rights (Right to fair trial) had been violated. This included not giving sufficient time to Sanader's legal team to prepare the defence, and exclusion of the public from crucial points in the trial while omitting those points from being covered in the court minutes.

3. UNCITRAL and ICSID Arbitrations

While the Croatian courts found the evidence of corruption convincing enough to hand out prison sentences to Sanader and Hernádi, the arbitral tribunals were not convinced.

The UNCITRAL proceedings, while starting later than the ICSID proceedings, resulted in a final award much sooner, in 2016. The arbitral tribunal arrived at a "confident conclusion that Croatia […] failed to establish that MOL did in fact bribe […] Sanader" as it failed to satisfy the standard of proof that the tribunal had deemed applicable, that one of 'reasonable certainty.' The tribunal considered that the testimony of the key witness in the case, Robert Ježi?, suffered from various implausibilities. The tribunal concluded that it had no choice but to deem Ježi? as "a witness unworthy of belief, who had a strong motive to shift the blame onto […] Sanader." The amendments to the Shareholder Agreement were thus left standing.

The ICSID proceedings wrapped up only this year. The ICSID tribunal found that the act of bribery was not proven, apparently basing its finding on the same grounds as the UNCITRAL tribunal, i.e., that Ježi? was an unreliable witness. The ICSID tribunal also found that Croatia violated the ECT as a result of its failure to liberalise the gas market between 2011 and 2014 and owing to the regulations that Croatia had introduced in 2014 to further regulate the gas market.

Unfortunately, the final award from the ICSID proceedings has not been made public as the parties had agreed to keep the text of the award confidential. However, MOL and the Government of Croatia did provide press releases, both of which seem to have been drafted by their respective 'spin doctors'. While Croatia was the losing party in the ICSID arbitration, the fact of the matter was that the ICSID tribunal granted approximately US$235 million in damages to MOL (including interest), which was a far cry from approximately US$1.1 billion that MOL was seeking to obtain. This allowed the Government of Croatia to portray the outcome of the arbitral proceedings as not entirely unfavorable to the country's interests while MOL's take on the matter was, although somewhat more reserved, a proud announcement to the market they had won the case.

One rather interesting question that inevitably arises in these kinds of cases is the extent to which arbitral tribunals should heed the decisions of national criminal courts. The general approach to this has been that a verdict rendered by a national court is in no way mandatory for an arbitral tribunal, but may be taken into account when the arbitrators assess the evidence.

4. The Standard of Proof in Corruption Cases

The MOL v. Croatia saga is yet another illustration of just how challenging it is to prove corruption, something that was at the heart of the dispute at hand.

A major challenge in proving corruption – either in arbitration or in court proceedings – is the fact that the act of corruption itself generally leaves little to no trace. As a result, setting the bar too high in terms of the standard of proof – e.g., 'beyond reasonable doubt' – would in essence mean that the vast majority of corruption cases would end with a finding that corruption was not proven. Given the universal condemnation of the very practice of corruption and its detrimental impact on all the aspects of a society, coupled with the difficulty of proving it, one may argue that the applicable standard of proof should lie somewhere below 'beyond reasonable doubt'.

At the same time, the finding of corruption generally results in very serious consequences for the party that has engaged in such an act. For example, in investment disputes, the investor's claim will generally be dismissed if the state proves that the investment had been procured through corruption. In criminal cases, the person found guilty of corruption may face a prison sentence. Thus, it is the very severity of corruption that lends itself to an argument that the standard of proof in corruption cases must be set higher than the mere 'balance of probabilities.'

In the world of arbitration, these opposing considerations have been a catalyst for lack of uniformity, with some tribunals applying 'a high standard of proof' or the standard of 'clear and convincing evidence'. One tribunal found the appropriate standard to be 'higher than the balance of probabilities but less than criminal standard of beyond reasonable doubt.' Some tribunals have gone for 'comfortable satisfaction standard,' while some, cognizant of the sheer difficulty of proving corruption, have adopted the 'balance of probabilities' standard. In the UNCITRAL proceedings involving Croatia and MOL, the arbitral tribunal seems to have fallen in the category of those requiring more than the mere 'balance of probabilities' by noting that its standard – that of 'reasonable certainty' – "is a matter of persuasion, and it may well be that for most minds becoming persuaded of something requires more than accepting that it is more likely than not."

5. Looking at the Bigger Picture

Given the duration and the high stakes involved in this case, it is only natural to ask if the MOL v. Croatia saga could have ramifications for the ISDS system in general, and especially so because of the existence of two opinionated camps as regards the legitimacy of the ISDS system.

Those coming to the defence of the ISDS system will point to the fact that, in contrast to the Croatian courts, two independent arbitral tribunals have not found the presented evidence sufficient for a finding that the bribery had taken place. Coupled with Judge Ambos's and Lord Anderson's Report, proponents of ISDS may use this to advance two arguments: (1) that this saga illustrates

the importance of ensuring that investors have access to a neutral forum outside of the purview of the host state's national courts, and (2) that this is relevant also in the intra-EU context, given the fact that both Croatia and Hungary are EU Member States. And as for the staunch critics of the ISDS system, they may use this saga as a case in point that the ISDS system is skewed in favour of the investors. After all, the courts of a full-fledged EU Member State had found the bribery had taken place, and instead of severe consequences for the investor, the ICSID tribunal ended up granting damages to the investor.

The diametrically opposed conclusions of the arbitral tribunals on the one side, and those of the Croatian courts on the other, seem to position this saga as a two-faced Janus looking towards both camps, giving each something to work with.

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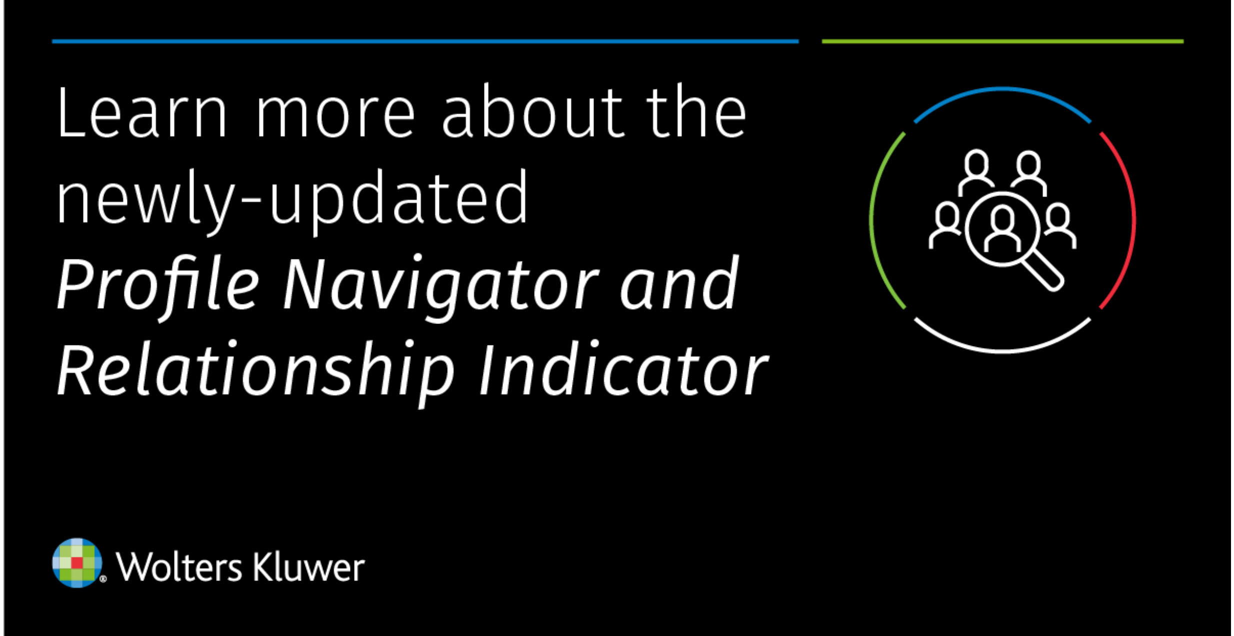

References

?1 Please note that this was an aggregate sentence that also covered another criminal offense, that of abuse of position.

?2 Ibid.

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