IN THE MATTER OF AN ARBITRATION **Arbitration No. XY/1010**

BEFORE THE COURT OF ARBITRATION OF THE HUNGARIAN CHAMBER OF COMMERCE AND INDUSTRY

BETWEEN:

(1) [POWER GENERATION LIMITED]
(UNITED KINGDOM)

First Claimant

(2) [THE POWER CORPORATION]
(UNITED STATES)

Second Claimant

AND

(1) [STATE ENERGY PRIVATIZÁCIÓS RÉSZVÉNYTÁRSASÁG]
(HUNGARY)

First Respondent

(2) [STATE ENERGY RÉSZVÉNYTÁRSASÁG]
(HUNGARY)

Second Respondent

DISSENTING OPINION

1. I greatly regret – after much upon which we have been in agreement – that I am unable to agree, in its final form, our Final Award in this arbitration. [Professor Philippe Alicante] has been an excellent Chairman of the Tribunal and I have enjoyed cordial relations throughout the conduct of this arbitration with him and my Co-Arbitrator [Dr Yegor Pécs].

2. This Dissenting Opinion, therefore, sets out my reasons why I am not able to agree the final terms of our Final Award in the hope that it will be of benefit to

the Parties to know why I have differed with my Fellow Arbitrators and to have before them Declarations which should enable them to avoid, in their future relations with one another, the difficulties that so far have beset them. For convenience I use the same terms in this Dissenting Opinion to identify the Parties and other matters, as are used in the Final Award. For example I refer to the Purchase and Sale Agreement of 4th July 1996 as "the Contract" and so forth.

3. The points, at which I respectfully part company with my Fellow Arbitrators, is upon how "Proven Losses" should be interpreted under the Contract and upon the rights of the First Claimant to institute arbitration proceedings and to obtain (albeit limited) the Declaratory Relief in it. On the former I believe "Proven Losses" should be given wider interpretation than Fellow Arbitrators wish to give to them and on the latter I believe the First Claimant was entitled to institute arbitration proceedings and is entitled to limited Declaratory Relief in these proceedings.

4. I also believe it is of paramount importance for the Tribunal to issue, as part of its Award, Declaratory Relief. In the first place, as I seek to show in this Dissenting Opinion, the First Claimant is entitled to Declaratory Relief - albeit more limited than it has sought in this arbitration. In the second place the Respondents are entitled to be strictly protected within the terms of the

Declaratory Relief granted to the First Claimant – this being best achieved, in my judgement, by granting them parallel Declaratory Relief. In the third place, since this Declaratory Relief is directed to defining the rights and obligations of the Parties in their future conduct with one another (which on the evidence before the Tribunal is likely to be for a number of years) the Parties will be in possession of explicit rulings on the substantive issues which have caused so much disagreement between them and so much time and expense. Thus it must be in the manifest best interests of the Parties to be able to move forward, with their rights and obligations clearly defined by the Tribunal, to deal with the extensive environmental 'clear-up' works ahead of them in a spirit of co-operation and trust.

5. As identified in the Final Award "Proven Losses" are defined in Article 1.1(bn) of the Contract. In this definition "Proven Losses" are defined as "all direct damages, losses, liabilities and costs" excluding "any contingent, consequential or indirect damages, losses, liabilities or costs". It is also stated within this definition that a "Proven Loss" can be "any one" of these matters. In my opinion each of these terms had, and were intended by the Parties to have, a different meaning within the overall definition of "Proven Losses". Most particularly, it seems to me, the term "liabilities" carries a different meaning from the terms "damages", "losses" and "costs". Since the Contract is governed by Hungarian law, the starting point is to consider these terms, and

particularly the term "liabilities", under Hungarian law. As advised by [Dr Yegor Pécs] the obligation, under Environmental Orders issued by the appropriate environmental authorities in Hungary, to carry out environmental 'clear-up' work cannot be construed as "liabilities" (which would have to be contractual liabilities) under Hungarian Law. I do not think however, we can stop there. Under Article 1.9 of the Contract we should construe the Contract under the English language which is "the binding and controlling language for all matters relating to the meaning or interpretation of this agreement". Hence I believe we should look at what meaning the Parties *intended* when drafting the definition of "Proven Losses" in the English language in a purchase and sale agreement which is structured under the concepts of English contract law. Thus we should construe "liabilities" in the wider sense used in the English language and as used in purchase and sale agreements constructed under English law. We should, therefore, construe 'liability' as being not only a liability for an accrued debt but also for a potential debt.[1]

[1] On this point I drew the attention of my Fellow Arbitrators to the authoritative text of Jowitt's Dictionary of English Law (Second Edition 1977) as follows: "**Liability**, the condition of being actually or potentially subject to an obligation, either generally, as including every kind of obligation, or, in a more special sense, to denote inchoate future, unascertained or imperfect obligations, as opposed to debts, the essence of which is that they are ascertained and certain. Thus when a person becomes surety for another, he makes himself liable, though it is unascertained in what obligation or debt the liability may ultimately result."
I also drew to the attention of my Fellow Arbitrators the recent Judgement in the Commercial Court of the English High Court (Total Liban SAL v Vitol Energy SA: 28.5.99) which confirmed the clear principle under English law that (citing authorities in support) 'liability' can arise 'without payment'.

6. The importance of defining 'liability' as distinct from 'damage' 'loss' or 'cost' of monies incurred and spent, brings sense into the interpretation of the provisions of the Contract where sense would not otherwise exist. Thus the First Claimant can be held to have served a valid notice, the *pre-requisite* for it obtaining *<u>any</u> indemnity relief*, under Article 7.4(a)(iii) at a time when no substantive environmental clear-up work could have taken place let alone paid for – it (or its subsidiary companies) only being under a 'liability' to undertake such works at some future date. Thus, on their side, the Respondents (under the terms of Article 7.4(b) of the Contract) has the right, after the receipt of this notice, "to undertake, conduct and control……the settlement or defence" of 'clear-up' costs being required under Environmental Orders. As pointed out in submissions to the Tribunal (and noted in paragraph 17(a) of the Final Award) for this provision to be of any use to the Respondents, as the Identifying Party, it must kick in at a time prior to the 'clear-up' costs having been undertaken and paid for. Above all the adoption of this interpretation of 'liability' achieves a clear and sensible division between the mechanism to set up environmental indemnity claims (a notice under Article 7.4(a) of the Contract) and the later "obligation to reimburse" under Article 7.3 of the Contract when the Company or the Principal Subsidiary (as the case may be) has carried out and paid for the works for which the First Claimant is then entitled to be reimbursed by the Respondents. It has been this difficulty – and the matter is

not easy – over the interpretation of "Proven Losses" which has led my Fellow Arbitrators, in my view, incorrectly to come to the view that the First Claimant was not entitled to institute arbitration proceedings and to obtain Declaratory Relief in them.

7. The First Claimant's right to institute arbitration proceedings rests in Article 12.9 of the Contract. The requirements here on the First Claimant is to satisfy the Tribunal, at the time of the institution of arbitration proceedings on 28th May 2001, (a) there was a dispute between the Parties (b) it was "arising out of or relating to" the terms of the Contract and (c) it was not "settled amicably within sixty (60) days" of the "receipt" of one Party's "written request to do so". Looking at the correspondence, (particularly the First Claimant's letter of 5th March 2001, the letter from both Respondents of 20th March 2001, and Smith & Jones' letter of 10th April 2001) it seems to me that the First Claimant has manifestly satisfied the provisions in Article 12.9 of the Contract. Moreover this correspondence also clearly shows there was a dispute which was quite fundamental to all the Parties on the indemnity issue. This dispute was over the validity of the First Claimant's notice under Article 7.4(a) of the Contract. As earlier stated in this Dissenting Opinion, and as is clearly set out in Article 7.4(a), it was a *pre-requisite* for the First Claimant obtaining *any indemnity relief* under the Contract for this notice to be served within the timetable set out in Article 7.4(a) and to be otherwise a valid notice.

8. Thus an examination of this correspondence also explicitly shows that the Respondents were *challenging the validity* of this notice (of 30th July 1999) on the grounds that it was not served in time and that "Proven Losses" were not "directly" falling on the First Claimant. Both of these challenges went to the root of the First Claimant's right to pursue its indemnity claim. If the notice of 30th July 1999 was invalid (as was being asserted by both Respondents right up to the commencement of the arbitration proceedings) the First Claimant had no right whatsoever to any indemnity under the Contract. Hence, it seems to me, that the First Claimant clearly had, on this issue, the right to institute arbitration proceedings and to seek a Declaration under Section 123 of Act III of 1952 on Hungarian Civil Procedure.

9. I have too to note that the Respondents have persisted in their challenges to the validity of this notice. For example the First Respondent raised again that this notice was out of time in paragraph 5 of its Final Submissions of 31st January 2003 and the Second Respondent raised again the challenges over losses not "directly" falling on the First Claimant in paragraphs 244, 245 and 246 of its Final Submissions of 31st January 2003 and in its oral submissions at the Arbitral Hearing.

10. As has been found in the Final Award this notice under Article 7.4(a) of the Contract was served in time and as it has also been found the First Claimant is entitled to be indemnified for losses suffered or incurred not "directly" by it but by the Company or Principal Subsidiary (see paragraphs 14(d), 22 and 23 of the Final Award) it seems to me, on the definition of 'liability' which I hold to be right, the Tribunal should make a Declaration in the First Claimant's favour but one more limited than sought by it. I cannot, however, agree to the First Claimant being entitled to the other Declaratory Relief it is seeking. At a time when substantially the environmental clear-up works have not taken place, let alone been paid for, it is premature to appoint the Independent Consultant and it is also premature to declare that the Respondent should pay for all "Proven Losses" before they are quantified or that the First Claimant is entitled to a Declaration that the Respondents pay to it "damages for repudiation of their liability to indemnify it for all Proven Losses" when it is too early for the Independent Consultant to be appointed and the environmental clear-up costs quantified.

11. Within the compass of this long running dispute between the Parties, there is a special reason why the Tribunal, in my view, should make a Declaration in favour of the First Claimant, in the terms I set out below, that the Respondents are under a duty to indemnify it for all damages, losses and costs incurred or suffered by the Company and the Principal Subsidiary. Despite repeated

assertions by the Respondents in correspondence, in pleadings in the arbitration and at the Arbitral Hearing that they remain "responsible" for the 'clear-up' costs of any pre-closing environmental contamination, the Second Respondent (as noted in paragraph 9 above) in its Final Submissions of 31st January 2003 specifically took the point that, under the terms of the Contract, there can be no "direct damages, losses, liabilities and costs" falling upon the First Claimant and entitling it to indemnity from the Respondents. The Second Respondent also takes the point, in these submissions, that the Company and the Principal Subsidiary (on whom the Environmental Orders are served and who are, therefore, immediately responsible for the consequential environmental 'clear-up' costs) cannot also invoke the indemnity provisions because neither of these companies were Parties to the Contract. Therefore the effect of construing the Contract in this manner (laying aside the alternative approach by the First Claimant in claiming that it is suffering, or has suffered, the 'direct loss' of the diminution in the value of its shareholding in the Company or Principal Subsidiary which, as shown at the Arbitral Hearing, presents a number of difficulties) would be to *nullify altogether* the indemnity provisions contained in Article 7.1 of the Contract - specifically the indemnity provisions for the environmental 'clear-up' costs contained in Article 7.1(e)(ii) of the Contract. The Final Award has held this is not right. It seems to me, therefore, that it is in the paramount interests of all Parties that the Tribunal should issue a Declaration on this issue, rather than just leave this point in the text of the Final

Award, so that, in the years ahead, when the Parties may have different managements, the position of the Tribunal on this very important issue is clearly and fully stated in a manner which remains binding on the Parties.

12. At the same time I believe the position of the Respondents should be protected. First there should be a parallel Declaration in the Respondent's favour to ensure that the Respondent's obligation to reimburse the First Claimant does not arise until the Company or the Principal Subsidiary has carried out and paid for the works upon which reimbursement is being sought. Also in order to avoid any further difficulties upon when the Parties can seek to appoint the Independent Consultant and upon what decisions he has power to make, I believe the Tribunal should make a further Declaration to deal with this issue.

13. If it could be formulated with sufficient precision I am also in favour of giving the Declarations informally sought by Counsel for the Second Respondent at the Arbitral Hearing relating to environmental costs being incorrectly claimed concerning the Györ and Miskolc II power plants when these costs had already been, or could be, factored into electricity charges or need not now be incurred or where losses should have been 'mitigated'. To achieve this, assistance would be needed from Counsel for the Second Respondent to put before the Tribunal the form of relief which is being sought here.

14. I do not believe that the granting to the First Claimant the Declaratory Relief, as I am suggesting should be granted, should alter the position on the payment of costs. I agree, therefore, with the Orders in the Final Award relating to the legal costs and expenses of the Parties and relating to the fees and expenses of the arbitration proceedings. I would just add that I think it would be inappropriate – and damaging – for the Parties working together, on a co-operative basis, in dealing with the substantial environmental clear-up works ahead of them, if there were to be Orders for payment of legal costs and expenses against one Party in favour of another.

ACCORDINGLY I BELIEVE THE ARBITRAL TRIBUNAL SHOULD DECLARE AND AFFIRM THAT:-

(1) The Respondents are under a duty to indemnify the First Claimant for all damages, losses and costs incurred or suffered by the Company and Principal Subsidiary consequent upon the Company's and Principal Subsidiary's compliance with Environmental Orders (relating to the Györ, Szekszárd and Miskolc II power plants) properly and lawfully issued by the appropriate environmental authorities in Hungary.

(2) The First Claimant is only entitled to reimbursement from the Respondents, under Article 7.3 of the Contract, when the Company or

the Principal Subsidiary (as the case may be) has carried out and paid for the works for which the costs are being sought.

(3) The First Claimant is not entitled under Article 7.1(e) of the Contract (through itself and/or the Company and/or Principal Subsidiary) to the [ ] costs claimed in respect of [ ].

(4) The First Claimant failed (through the Company and Principal Subsidiary) in its duty, under Article 7.5 of the Contract, to mitigate the costs arising under Article 7.1(e) of the Contract (by taking all reasonable steps in a timely manner to reduce or remove liability for such costs) in respect of [ ].

(5) In the event of a dispute arising between the Parties upon whether the Respondents are required to reimburse the First Claimant for any item of costs, as identified in Declaration (1) above, and/or upon the quantification of such reimbursement, the First Claimant and the Respondents are under a duty, no earlier than when the Company or Principal Subsidiary enters into a contract for the performance of remedial work related to the environmental orders and no later than when payment falls due pursuant to such a contract, promptly to agree upon the appointment of the Independent Consultant. For the avoidance

of doubt the Independent Consultant has power to decide any of the matters identified in the last sentence in the first paragraph of paragraph 23 of the Final Award.

15. While in this Dissenting Opinion I do respectfully dissent from my Fellow Arbitrators on the definition of "Proven Losses" and upon the First Claimant's right to limited Declaratory Relief, I hope that much of this Dissenting Opinion will be seen as taking forward the Final Award as so admirably prepared by our Chairman. Similarly I hope this Dissenting Opinion will be seen by the Parties as leading them forward out of the disputes which have bedevilled them to a future of co-operation between them. If they wish to do so, they could, for example, reach an Agreement between one another on the basis of the Declarations (as drafted as above or suitably amended) which I propose in this Dissenting Opinion but which are not in the Final Award.

DAVID HACKING

CO-ARBITRATOR

April 2003