INTERNATIONAL CENTRE FOR SETTLEMENT OF INVESTMENT DISPUTES
WASHINGTON, D.C.

In the matter between

HRVATSKA ELEKTROPRIVREDA D.D.
(Claimant)

and

THE REPUBLIC OF SLOVENIA
(Respondent)

(ICSID Case No. ARB/05/24)

DECISION ON THE TREATY INTERPRETATION ISSUE

Members of the Tribunal

The Hon. Charles N. Brower, Arbitrator
Mr Jan Paulsson, Arbitrator
Mr David A. R. Williams, Q.C., President

Secretary of the Tribunal

Ms Aïssatou Diop

Representing the Claimant

Mr Robert W. Hawkins
Mr Stephen M. Sayers
Hunton & Williams LLP

Representing the Respondent

Mr Stephen Jagusch
Mr Mark Levy
Mr Laurent Gouiffès
Mr Anthony Sinclair
Allen & Overy LLP

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I. THE PARTIES AND THE NATURE OF THEIR DISPUTE

CLAIMANT: HRVATSKA ELEKTROPRIVREDA, D.D.

1. The Claimant, Hrvatska elektroprivreda, d.d. ("HEP"), is the national electric company of Croatia. It was formed in July 1990 pursuant to the 1990 Electricity Act by the consolidation of 119 formerly independent electricity organisations. In 1994 HEP's status changed from a state-owned company to a joint-stock company. From 1994 to the present 100% of the stock in HEP has been owned by the Government of Croatia.[1]

RESPONDENT: THE REPUBLIC OF SLOVENIA

2. The Respondent, the Republic of Slovenia ("Slovenia"), came into existence on 25 June 1991 when the Slovenian parliament declared independence from the former Socialist Federal Republic of Yugoslavia.[2]

OTHER ENTITIES RELEVANT TO THE DISPUTE

The Krško Nuclear Power Plant

3. The socialist republics of Slovenia and Croatia agreed in the 1970s to jointly construct and operate a nuclear power plant in Slovenia, the Krško Nuclear Power Plant ("Krško NPP"). The construction of the Krško NPP commenced in 1974. The Krško NPP has been in commercial operation since 1983. It is located just outside of the town of Krško in south-eastern Slovenia, approximately 15 kilometres west of the border between Croatia and Slovenia.[3]

Nuklearna Elektrana Krško vu

4. Nuklearna elektrana Krško ("NEK"), a limited liability company, is a "work-organisation"; it was established as a joint venture by the national electricity companies of Croatia and Slovenia in 1974 to build and operate the Krško NPP. NEK applied for and holds the licence to operate the Krško NPP.

Elektro-Slovenija, d.o.o. Ljubljana

5. Elektro-Slovenija, d.o.o. Ljubljana ("ELES-GEN") is a wholly-owned subsidiary of Elektro-Slovenija, d.o.o. ("ELES"), the national electric power transmission company of Slovenia.

THE NATURE OF THE DISPUTE

6. This case arises out of a dispute between HEP and Slovenia concerning the ownership and operation of the Krško NPP. The plant is a significant national power resource for both countries.

[1] Claimant's Memorial on the Merits ("Claimant's Memorial"), para 13

[2] Claimant's Memorial, para 14

[3] Claimant's Memorial, paras 15-16

7. The Krško NPP was designed and constructed in the 1970s with funds contributed equally by the national power industries of the Socialist Republics of Slovenia and Croatia when they were both still part of the former Yugoslavia. The costs of design, development and construction totalled US $1.2 billion. HEP is the successor-in-interest of the original Croatian investors that contributed US $600 million to design and construct the Plant. The Krško NPP constituted the single largest foreign investment of any Croatian company at the time.

8. The financing, construction, operation, management and use of the Krško NPP was regulated by four inter-related agreements entered into by the Socialist Republics of Slovenia and Croatia, together with representatives of their national power industries, one each in 1970 and 1974 and two in 1982 (the "Governing Agreements").

9. The cornerstone of the Governing Agreements was the principle that the co-investors were to be 50:50 partners in all aspects of the plant construction, management, use and operations. Each co-owner, thus, had the right to receive 50 percent of the power output of the plant at prices to be determined in accordance with the Governing Agreements. This principle became known as the "parity principle."

10. Slovenia and Croatia both declared their independence in 1991. During the next several years, the Slovenian Government adopted a series of measures that were viewed by HEP as inconsistent with the parity principle and the basic provisions of the Governing Agreements. On July 30, 1998, the Slovenians disconnected the electricity lines from the Krško NPP to Croatia and terminated all electricity deliveries to HEP, and issued a Governmental "Decree" which HEP claims affected its rights as a 50 percent owner and manager of the plant.

11. Following Slovenia's displacement of HEP from its role as a 50 percent owner of the Krško NPP, the governments of the two countries entered into negotiations aimed at restoring HEP's rights. Those talks eventually stalled over financial issues. In mid-2001, however, Dr Goran Granic, the Deputy Prime Minister of Croatia, proposed a settlement approach that ultimately broke the deadlock. Dr Granic suggested that, rather than continuing to debate past financial differences, the parties, in essence, should "wipe the slate clean" as of an agreed date in the future. Under Dr Granic's proposal, all of the parties' claims up to this agreed date would be waived and, on that agreed date, deliveries of electricity to HEP from the Krško NPP were to be restored. At a meeting of the Prime Ministers of Croatia and Slovenia held in Rijeka, Croatia on June 9, 2001, the Prime Ministers formally endorsed Dr Granic's settlement approach, and they agreed upon June 30, 2002 as the date for resumption of deliveries of electricity to HEP, and the date through which all financial claims were to be waived. These agreements were recorded in the Agreement Between the Government of the Republic of Croatia and the Government of the Republic of Slovenia on Regulation of the Status and Other Legal Relations Regarding the Investment, Use, and Dismantling of Nuclear Power Plant Krško (the "2001 Agreement")[4].

12. HEP contends that Slovenia failed to restore HEP's rights as a 50 percent owner of the Krško NPP or to resume electricity deliveries from the plant by June 30, 2002, as agreed in the 2001 Agreement. Slovenia did not ratify the 2001 Agreement until late

[4] Exhibit C-185 (a copy of the 2001 Agreement is attached to this Decision.)

February of 2003, and Slovenia did not resume deliveries of electricity from the Krško NPP to HEP until April 19, 2003.

13. In this proceeding, HEP seeks compensation for the financial losses it alleges that it has suffered as a result of Slovenia's failure to resume deliveries of electricity from the Krško NPP to HEP by the 30 June, 2002 date established in the 2001 Agreement. HEP advances two independent legal bases for its claim.

14. First, HEP alleges that Slovenia's termination of electricity deliveries to HEP on July 30, 1998, together with the issuance that same day of a Decree removing HEP's rights as a 50 percent owner of the Krško NPP, violated HEP's right as an investor under Articles 10(1) and 13 of the Energy Charter Treaty (the "ECT Claims"). HEP contends that those violations continued until deliveries of electricity were restored to HEP on April 19, 2003. HEP says that in the 2001 Agreement, properly construed, it agreed to waive its ECT claims accruing up to June 30, 2002. HEP contends it did not, however, waive its ECT claims that accrued during the period July 1, 2002 to April 19, 2003.

15. Separately, and independently, HEP asserts a claim against Slovenia for breach of its obligation under the 2001 Agreement to restore electricity deliveries to HEP from the Krško NPP by June 30, 2002.

II. PROCEDURAL HISTORY LEADING TO PROCEDURAL ORDER (NO 4) OF 6 OCTOBER 2008 DIRECTING DETERMINATION OF THE TRUE INTERPRETATION OF THE 2001 AGREEMENT ("THE TREATY INTERPRETATION ISSUE")

16. The Claimant is represented by Messrs Robert W. Hawkins and Stephen M. Sayers of Hunton and Williams LLP, 1900 K Street, N.W., Washington, D.C. 20036, United States. The Respondent is represented by Messrs Stephen Jagusch, Mark Levy, Laurent Gouiffès and Anthony Sinclair of Allen & Overy LLP, One New Change, London EC4M9QQ, United Kingdom.

17. The Request for Arbitration was filed on 4 November 2005 by the Claimant.

18. On 27 February 2006, the parties entered into an Agreement on Constitution of the Tribunal[5] under Rule 2 of the ICSID Arbitration Rules ("ICSID Rules"). Pursuant to clauses 3, 4 and 8 of the Agreement, the Tribunal was to consist of three arbitrators, one arbitrator to be appointed by each party, and the two party-appointed arbitrators to choose and appoint the President of the Tribunal. Accordingly, the Claimant appointed the Honorable Charles Brower and the Respondent appointed Mr Jan Paulsson. Judge Brower and Mr Paulsson together appointed as President of the Tribunal Mr David A. R. Williams, QC.

19. After all three arbitrators had accepted their appointments, the Acting Secretary-General by letter dated 20 April 2006 informed the parties that the Tribunal was deemed to be constituted and the proceeding to have commenced on that day,

[5] Agreement on Constitution of the Tribunal in HEP v. Slovenia (ICSID Case No. ARB/05/24), submitted to the Centre under cover of letter of 28 February 2006.

pursuant to Rule 6(1) of the Rules of Procedure for Arbitration Proceedings (Arbitration Rules) of the Centre (the "ICSID Arbitration Rules").

20. The Tribunal held its first session in London on 3 July 2006, in accordance with ICSID Arbitration Rule 13(1). Procedural matters were discussed and agreed. All conclusions reached were reflected in the Minutes of the First Session.

21. The Claimant filed its Memorial on the Merits on 10 November 2006.

22. By letter dated 8 December 2006, the Respondent notified the Claimant and the Tribunal that it objected to the jurisdiction of the Centre and to the competence of the Tribunal to decide the claims set out in the Claimant's Memorial on the Merits. The Respondent sought that its objections to jurisdiction be determined as a preliminary matter, and separately from the merits of the dispute. Furthermore, the Respondent proposed that the date for filing its Memorial on Objections to Jurisdiction and Admissibility be moved to 30 March 2007.

23. On 14 December 2006 the Tribunal invited both parties, on a provisional basis and subject to its decision on bifurcation, to consider an appropriate date for a hearing on jurisdiction should the Tribunal decide to bifurcate the proceeding.

24. The Claimant, by letter dated 19 December 2006, replied to the Respondent's objections to jurisdiction and bifurcation. The Claimant objected to the Respondent's suggested new date for filing its Memorial on Objections to Jurisdiction and Admissibility on the basis that it was contrary to the timetable already consented to by the parties at the first session of the Tribunal.

25. On 22 December 2006 the Tribunal directed the Respondent to file, by 19 January 2007, a reply to the Claimant's letter of 19 December 2006. The Respondent replied on 22 December 2006, reiterating its request for bifurcation and for leave to file on 30 March 2007 its Memorial on Objections to Jurisdiction and Admissibility. The Respondent noted that the timetable set out in the Minutes of the First Session had been conditional on the Respondent not raising, as a preliminary matter, any objections to jurisdiction and admissibility.

26. Responding to the Tribunal's letter of 14 December 2006, the Claimant stated that it was unable to propose a procedural timetable for a first round of proceedings whilst the Tribunal's decision on the Respondent's request for bifurcation was still pending. In a further letter dated 5 February 2007 the Claimant submitted its proposed procedural timetable. In order that its proposals be implemented, the Claimant suggested that the Tribunal hold a telephone conference between the parties.

27. The Secretary of the Tribunal notified the parties by e-mail on 15 February 2007 that the Tribunal had decided, under ICSID Arbitration Rule 41(4), to reject the Respondent's request for bifurcated proceedings dealing with its jurisdictional objections first and separately from the merits of the dispute.

28. In relation to discovery, the Respondent submitted to the Claimant a request for the production of documents on 26 March 2007. The parties then exchanged some correspondence on the issue. On 6 June 2007 the Tribunal issued an Order on Respondent's requests for production of documents. On 21 June 2007 the Tribunal

issued Procedural Consent Order No.2 setting out a revised timetable for document production and the submission of pleadings by the parties.

29. The Respondent filed its Counter-Memorial and Memorial on Objections to Jurisdiction and Admissibility on 6 July 2007.

30. The Claimant filed an amended request for the production of documents on 23 August 2007. Subsequently, by letter dated 25 September 2007, the Claimant applied to the Tribunal for an order directing that the Respondent produce several outstanding categories of documents that had been requested.

31. Further to the parties' respective submissions on the Claimant's document request, the Tribunal, by e-mail dated 9 November 2007, requested that the parties provide additional comments on the progress of their production of certain documents the requests for which were still in dispute.

32. The Claimant filed its Reply Memorial on the Merits on 10 December 2007.

33. On 25 January 2008 the Tribunal issued an Order on Claimant's Requests for Production of Documents. Following the Claimant's revised request for document production of 4 February 2008 and the ensuing submissions of the parties thereon, the Tribunal issued an Order on Claimant's Revised Request for Production of Documents on 1 April 2008.

34. The Respondent filed its Rejoinder on 7 April 2008.

35. In preparation for the hearing, the parties notified the Tribunal by separate e-mails dated 11 April 2008 of those witnesses and experts they each wished to cross examine at the May 2008 oral proceeding in Paris.

36. The Tribunal issued a Procedural Order on 14 April 2008 communicating the schedule for the hearing set to commence on 5 May 2008. A telephone conference was held on 21 April 2008 between the Tribunal and the parties to address procedural matters relating to the hearing. The agreed list of documents was issued on 1 May 2008. The parties filed their respective Pre-Hearing Submissions on 2 May 2008.

37. The hearing commenced on 5 May 2008 at the offices of the World Bank in Paris.

38. Previously, on 25 April 2008, Allen & Overy, counsel for the Respondent, had submitted the Respondent's list of persons who would be attending the substantive hearing in Paris, including a Mr David Mildon, QC of Essex Court Chambers, London, where the President of the Tribunal is a door tenant. The Claimant expressed concern at the addition to the Respondent's legal team of counsel affiliated with the same chambers as the President of the Tribunal at such a late stage in the proceedings, and requested that, pursuant to ICSID Arbitration Rules 19 and 39, the Tribunal order that the Respondent refrain from using the services of Mr Mildon, QC. Following written submissions from the parties, the Tribunal ruled that Mr Mildon, QC, could not continue to participate as counsel in the case.

39. Following the Tribunal's ruling on the participation of Mr Mildon, QC, the hearing proceeded in the afternoon of 6 May 2008 on all except certain specified matters relating to liability and quantum. Those matters were reserved for a future hearing.

40. On 30 May 2008 the Respondent made an application in respect of the ECT Claims requesting that:

> the arbitral tribunal determine and adjudge that the ECT [C]laims need not be determined or alternatively that the proceedings in relation to them should be stayed until such time as the Tribunal can finally rule on whether it is necessary to determine them. This is because the ECT [C]laims are, on the basis of how HEP has put its case and in any event as a matter of irrefutable logic, legally and factually irrelevant to the full and final determination of HEP's claims in this proceedings.

41. Simultaneously, the Respondent filed an application for further disclosure to be considered by the Tribunal in the event that the Respondent's application in relation to the ECT Claims was denied. On 16 June 2008 the Claimant lodged its opposition to the Respondent's application in respect of the ECT Claims. On the same day, the Tribunal issued Procedural Order (No.3) with directions for the second phase of the hearing.

42. On 8 July 2008 the Respondent replied to the Claimant's opposition to the Respondent's application in respect of the ECT Claims. The Claimant filed a rejoinder on 17 July 2008 concerning the two applications filed by the Respondent on 30 May 2008.

43. By e-mail dated 28 July 2008, the President of the Tribunal informed the parties that, having carefully considered the Respondent's application in respect of the ECT claims, it had come to the provisional view that it should focus on determining the fundamental issue of the true interpretation of the 2001 Agreement (the "Treaty Interpretation Issue"). The President of the Tribunal concluded that the question of liability turned on the Treaty Interpretation Issue, which should be determined first in the proceedings. Each party was requested to advise the Tribunal of whether it would agree to a hearing to determine the Treaty Interpretation Issue and to make submissions on how the Treaty Interpretation Issue should be framed.

44. By letter dated 8 August 2008, the Respondent agreed with the Tribunal's suggestion that a hearing be held to determine the Treaty Interpretation Issue. The Claimant responded on 14 August 2008, contending that it was not necessary to hold separate hearings on the Treaty Interpretation Issue, whether Slovenia had violated the ECT and on quantum. Instead, it submitted that the ECT claims should be determined alongside the Treaty Interpretation Issue.

45. In Procedural Order (No.4) dated 6 October 2008 the Tribunal concluded that, between the claims under the 2001 Agreement and the ECT Claims, it was preferable to decide first the question of whether the former claims were tenable under the 2001 Agreement. The Tribunal noted that a ruling on the matter favourable to the Claimant would potentially obviate the need to consider the ECT Claims. Similarly, a ruling favourable to the Respondent could preclude the ECT Claims. Nonetheless, the Tribunal stated that if the Claimant failed on its claims under the 2001 Agreement, and it was not precluded by the Tribunal's ruling from pursuing the ECT Claims further, it would be able to do so in the 2009 hearings. Pursuant to Article 44 of the ICSID Convention and its inherent powers the Tribunal ordered:

> (1) The question as to the true interpretation of the 2001 Treaty (ie, HEP exhibit 185, the Agreement between the Government of the Republic of Croatia and the Government

of the Republic of Slovenia on Regulation of Status and Other Legal Relations Regarding the Investment, Use and Dismantling of Nuclear Power Plant Krško dated December 19, 2001) be the subject of a hearing at the World Bank Headquarters, Avenue Iena, Paris, France commencing at 10.00 am on Monday 24 November and concluding at 5.00pm on Tuesday, 25 November 2008.

(2) Following the hearing the Tribunal will determine whether the Claimant is entitled to succeed on its claim as to liability ie, its assertion that it is entitled to compensation or damages under the 2001 Treaty measured by the difference between the cost to it of electricity during the period 1 July 2002 until 19 April 2003 and the (allegedly lower) cost to it had the electricity been supplied to it by the Respondent based on the substantive provisions of the Treaty.

46. On 24 October 2008 the Claimant filed its Submissions on the Respondent's Liability under the 2001 Agreement. The Respondent filed its Submissions on the Treaty Interpretation Issue on 14 November 2008. The Claimant filed its Reply Submissions on the Respondent's Liability under the 2001 Agreement on 19 November 2008.

47. Pursuant to Procedural Order (No.4), a hearing on the Treaty Interpretation Issue was held at the World Bank Headquarters, Paris between 24-25 November 2008.

48. On 3 December 2008 the Respondent requested the Tribunal's permission to introduce a new exhibit, Exhibit No. 326. By e-mail dated 4 December 2008 the Claimant objected to the Respondent's attempt to introduce Exhibit No. 326.

49. In response to an invitation from the Tribunal during the hearing on 25 November 2008, the Claimant filed its Submissions on Implied Treaty Terms on 12 December 2008. One the same day, the Respondent also filed its Submissions on *Case A15*, responding to the Tribunal's request that the parties comment on *Islamic Republic of Iran v. The United States of America,* Partial Award No.529-A15-FT, 6 May 1992 (*"Case A15.")* [6]

50. On 10 February 2009, the Tribunal issued a ruling admitting the Respondent's proposed Exhibit No.326. The Claimant made further Submissions on the Respondent's "[A]cquiescence [A]rgument" and Exhibit No. 326 on 3 March 2009. On the same date the Respondent also made further Submissions on Acquiescence and Exhibit No.326.

III. SUMMARY OF THE FACTS

51. The material facts established by the parties' pleadings, the documents, and the relevant evidence are set out below. Where there is disagreement between the parties as to the course of events, or the reasons behind the events, that disagreement is noted. If one party has asserted a fact and the other has not disputed it, the fact has been taken as uncontested.

THE GOVERNING AGREEMENTS

52. In the late 1960s, Slovenia and Croatia were often affected by power shortages. The two republics agreed to jointly build two nuclear power plants, one in Slovenia and,

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[6] 28 Iran-U.S. C.T.R 112

following its construction, one in Croatia.[7] However, due to a changing political climate following the nuclear accident in Chernobyl, Ukraine, only the nuclear power plant situated in Slovenia was ever built.[8]

53. The contractual framework for the construction and operation of the Krško NPP is outlined by the four Governing Agreements: the Agreement of the Socialist Republic of Croatia and the Socialist Republic of Slovenia on Construction and Use of Krško Nuclear Power Plant dated October 27, 1970 (the "1970 Agreement")[9]; the Agreement on Pooling of Resources for Joint Construction and Joint Exploitation of Krško Nuclear Power Plant dated March 22, 1974 (the "1974 Pooling Agreement");[10] the Annex of the Agreement on Pooling of Resources for Joint Construction and Joint Exploitation of Krško Nuclear Power Plant dated April 16, 1982 (the "1982 Annex to the Pooling Agreement");[11],and the Self-Management Agreement on Regulation of Mutual Rights and Liabilities Between the Incorporators and Krško Nuclear Power Plant dated April 16, 1982 (the "1982 Self-Management Agreement").[12]

The 1970 Agreement Established the Parity Principle

54. Pursuant to the 1970 Agreement, Croatia and Slovenia committed to "support the action of [the] electric-power industries and other interested organizations from Croatia and Slovenia as regards the construction of [the] joint nuclear power plant" and to "provide all the necessary assistance and support necessary to achieve the goal of the said action." Clause 4 of the 1970 Agreement incorporates the "parity principle":

> The Republics deem that the joint investors from both Republics should participate in financing of construction of [the] joint nuclear power plant in equal parts and that their rights and liabilities should reflect such equal parts.
>
> The same principles should apply in establishing the rights and obligations during the operation of the joint nuclear power plant.

55. Clause 7 of the 1970 Agreement provided that the co-founders would be jointly liable for the procurement and repayment of foreign loans.

56. Clause 9 provides as follows:

> The Republics agree and understand that, in the case the economic measures and instruments are introduced in any of the two Republics, which adversely affect the construction or use of the joint nuclear power plant, as compared to the conditions in force at the beginning of its construction, such measures and instruments shall not have any effect on the rights and liabilities of the investors from the other Republic.

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[7] Clause 3, 1970 Agreement, Exhibit C-1

[8] Slovenia's Counter-Memorial and Memorial on Objections to Jurisdiction and Admissibility (Respondent's Counter-Memorial"), paras 15-16, 24-27

[9] Exhibit C-1

[10] Exhibit C-2

[11] Exhibit C-3

[12] Exhibit C-4

57. The specific details of the business arrangements were left to be determined by the joint investors, the electric power companies of Croatia and Slovenia, "in such a way that... the investors practically, directly or indirectly, have the rights to such part of the capacity of joint nuclear power plant which is directly related to the amount of their investment."[13]

The 1974 Pooling Agreement Continued the Parity Principle

58. The 1974 Pooling Agreement was concluded on 22 March 1974 as the construction of the plant was about to begin between Elektroprivreda Zagreb, on behalf of the electric power companies of Croatia, and Savske Elektrarne Ljubljana, on behalf of electric power companies of Slovenia. Clause 2 of the 1974 Pooling Agreement stated that the parties would: (i) permanently pool the resources for construction and start-up of the Krško NPP; and (ii) incorporate a joint venture company, NEK, through which they would jointly build, operate and use the Krško NPP.

59. Each of the Parties would cover 50% of the construction expenses and be liable for 50% of the total liabilities of NEK.[14] Concerning the management structure of NEK, the 1974 Pooling Agreement stipulates that the Management Board would have 22 members, with each party appointing 10 members and the parties jointly appointing two additional members.[15] Clause 21.3 stipulates that NEK "shall take care to fill the managerial and the key work posts in such a manner that the Parties are represented in equal proportions."

60. Regarding the exploitation of the Krško NPP, the 1974 Pooling Agreement stated that: (i) each of the parties would be entitled to receive 50% of the total available power and electricity generated by the plant;[16] (ii) the parties would jointly establish the price of power from Krško NPP, and any profit would be allocated between the Parties in a 50:50 proportion;[17] and (iii) all risks associated with the operation of Krško NPP would be shared 50:50 by the parties.[18]

61. The first paragraph of Clause 6.1 of the 1974 Pooling Agreement "Liabilities of Incorporators towards NE Krško, Company in the Process of Incorporation" reads:

> Each of the Parties shall be liable to NE Krško, company in the process of incorporation, up to the amount of 50% of the total liabilities.

62. HEP claims that Clause 6.1 of the 1974 Pooling Agreement provided a cross-guarantee for unpaid liabilities of NEK, i.e. each party was to be liable for 50% of the total liabilities of NEK.[19] Slovenia disagrees. It considers that Clause 6.1 only applied to liabilities of the parties until the incorporation of NEK.

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[13] Clause 11, 1970 Agreement

[14] Clauses 3.4, 3.5 and 6.1, 1974 Pooling Agreement

[15] Clause 9.1.3, 1974 Pooling Agreement

[16] Clause 17.1.2, 1974 Pooling Agreement

[17] Clause 17.2.6, 1974 Pooling Agreement

[18] Clause 17.3, 1974 Pooling Agreement

[19] Claimant's Memorial, para 32

63. Clause 17.1.2 of the Agreement reads:

> In case the Party from SR Slovenia fails to provide to the Party from SR Croatia the use of power and electricity from NE Krško pursuant to provisions hereof because it has used the power and electricity itself, it shall compensate to the Party from SR Croatia the difference in price of power plants or from other territories due to such failure, including the electricity acquired abroad, taking into account the reasonable nature of offers for supply as regards the price.

Finally, the 1974 Pooling Agreement provided for arbitration for the settlement of any disputes arising between the Parties in connection to an Agreement.[20]

The 1982 Annex to the Pooling Agreement Further Implemented the Parity Principle

64. On 16 April 1982, by which time construction of the Krško NPP was completed and operations at the Plant about to begin, the electric companies of Croatia and Slovenia entered into the 1982 Annex to the Pooling Agreement. The main reason for this annex was to update the 1974 Pooling Agreement and to bring it into conformity with the Associated Labour Act (the "ALA"), legislation passed by the Federal Republic of Yugoslavia to govern "work organisations" such as NEK. The 1982 Annex to the Pooling Agreement did not change in any material respect the basic structure of the joint venture relationship established by the 1974 Pooling Agreement.

The 1982 Self-Management Agreement Extended the Parity Principle

65. Together with the 1982 Annex to the Pooling Agreement, the 1982 Self-Management Agreement was entered into on 16 April 1982 between: (i) the Associated Electric Power Industry Companies of Slovenia, Maribor; (ii) the Association of Electric Power Industry Companies of Croatia, Zagreb; and (iii) Krško NPP, in the process of incorporation.[21] The bulk of the 1982 Self-Management Agreement is devoted to: (i) a delineation of the rights and liabilities of the national electricity companies with respect to electricity produced at the Krško NPP;[22] (ii) NEK's obligations with respect to Krško NPP's operations; and (iii) the method of calculation of the price of electricity.[23]

66. According to the 1982 Self-Management Agreement, Krško NPP was to supply electricity only to the electricity companies of the two countries in equal proportions,[24] and the price of electricity was to be mutually determined by the two companies for each business year in advance.[25] The price of electricity was to include elements such as costs, investment maintenance and depreciation.[26] The costs and income estimate was to encompass "costs of nuclear fuel and other costs relating to

[20] Clause 22, 1974 Pooling Agreement

[21] The Agreement stipulates that it is entered into between the employees of these companies (according to the system of social ownership).

[22] Clause 5, 1982 Self-Management Agreement

[23] Clauses 7 and 8, 1982 Self-Management Agreement

[24] Clause 6.3, 1982 Self-Management Agreement

[25] Clause 7.1, 1982 Self-Management Agreement

[26] Clauses 7.3 and 8.4, 1982 Self-Management Agreement

the aforementioned fuel [...] other material costs [...] investment maintenance [...] depreciation [...] income."[27]

67. The 1982 Self Management Agreement provided for the appointment of the Board of Directors ("BoD") and the Management Board. The BoD was to consist of twelve members, four to be appointed by the electricity companies of each of the two Republics, and four to be appointed by NEK. The Management Board was to consist of six members, three appointed by the Slovenian companies and three from the Croatian ones. The Slovenian national electricity companies were to appoint: (i) the Chairman of the Management Board; (ii) the Manager of the Economic and Finance Division; and (iii) the Manager of the General, Legal and Personnel Division. The Croatian national electricity companies would appoint: (i) the Vice-Chairman of the Management Board; (ii) the Manager of the Engineering Division; (iii) the Manager of the Commercial Division.[28]

68. Clause 15.1 provided for the resolution of disputes by arbitration of the Association of Yugoslav Electric Power Industry. Clause 16.3 provided that "none of the participants in this Agreement may transfer the rights and obligations resulting from this Agreement without the consent of other participants".

69. Slovenia emphasises that the Governing Agreements are to be understood and interpreted within the context of the socialist political and legal regime of Yugoslavia at the relevant time. The Krško NPP has never been in the ownership of HEP. NEK was a "work organisation", a "unique embodiment of the Yugoslav socialist legal system". It was "socially-owned" and therefore had no owners. Instead, it was managed by its workers. The two groups of electricity companies were only the co-founders of the plant, and had specific rights and liabilities according to the Governing Agreements (e.g. to use an electricity share from the Krško NPP and to participate in the joint decision-making organs).[29] They were not, however, co-owners of Krško NPP, as HEP argues.

70. The Governing Agreements did not deal with the issue of disposal or storage of radioactive waste. The only relevant provision is Clause 17.4.1 of the 1982 Annex to the Pooling Agreement:

> The Parties shall take all measures to provide, upon completion of construction of NE Krško, the security measures for prevention of possible adverse consequences for the human environment.
>
> The costs of performance of measures from the previous paragraph, together with the costs arising from disposal of nuclear fuel and radioactive waste shall be borne by the Parties from each Republic in proportion 50:50.

71. Slovenia considers that the intention was that each State would be responsible for the removal and safe storage of waste of the plant on its territory. This was the reason why no relevant provisions were included in the Governing Agreements. According to Slovenia, "in the event that the second plant was not built, it was evident that

[27] Clause 8.4, 1982 Self-Management Agreement

[28] Clauses 10.2 and 12, 1982 Self-Management Agreement

[29] Respondent's Counter-Memorial, paras 19, 21-22

responsibility would be shared between the parties, in line with the parity principle as envisaged in the 1970 Agreement."[30]

THE OPERATION OF NEK IN THE 90S AND THE DIFFERENCES BETWEEN THE PARTIES

72. Croatia submits that its investment in Krško NPP amounts to US$600m. Slovenia contests this amount.[31]

73. Commercial operations at Krško NPP commenced in January 1983.

74. In July 1990, 119 independent electricity organisations in Croatia were consolidated to form HEP, a state-owned company. As the legal successor of the Croatian parties to the 1974 and 1982 Agreements, HEP assumed all of the rights and obligations of the Croatian investors under the Governing Agreements.[32]

75. On 25 June 1991 Slovenia and Croatia both declared independence from the former Federal Republic of Yugoslavia. Shortly afterwards, differences began to emerge between the Government of Slovenia on the one hand, and HEP and the Government of Croatia on the other, with regard to the operation and status of the Krško NPP and the application of the Governing Agreements.

76. HEP submits that the Government of Slovenia has taken over the rights of the Slovenian incorporators of the Krško NPP. At the end of 1995 the General Manager of HEP wrote to ELES and Savske Elektrarne Ljubljana po ("Savske Elektrarne"), two of the major electricity companies in Slovenia, requesting them to appoint the representatives of the Slovenian Incorporator who would participate in negotiations. In their responses, the two companies stated that the rights of incorporators has been taken over by the Republic of Slovenia.[33]

77. In early 1994, the Presidents of Slovenia and Croatia agreed that legal and status questions regarding the Krško NPP needed to be regulated with a new inter-State agreement.[34] The negotiating process started in March 1994. Slovenia's position was that the Governing Agreements did not acquire the status of a treaty when Slovenia and Croatia became independent sovereign States. Moreover, Slovenia maintained that many of the existing provisions of the Governing Agreements were no longer appropriate in the new political and legal climate. Croatia thought that the Governing Agreements should be elevated to the level of a treaty or bilateral contract and should continue to regulate Krško NPP matters.[35] This issue was not resolved until the signature of the 2001 Agreement on 19 December, 2001.

[30] Respondent's Counter-Memorial, para 23

[31] Respondent's Counter-Memorial, fn 3

[32] Claimant's Memorial, para 59

[33] Exhibits C-43 and C-89; Claimant's Memorial, paras 77, 78

[34] Respondent's Counter-Memorial, para 183

[35] Respondent's Counter-Memorial, para 184

The Creation of a Decommissioning Fund

78. In December 1994 the Slovenian Parliament adopted a "Law on the Fund for Financing the Decommissioning of the Krško Nuclear Power Plant and the Disposal of Radioactive Waste of the Krško Nuclear Power Plant".

79. Croatia states that "at no time did the Government of Slovenia ever consult with HEP, or any other party from Croatia, regarding any of the financial, legal, administrative or other requirements imposed by this Law."[36] This law offered Slovenia very wide powers concerning the establishment of the decommissioning programme in breach of the Governing Agreements' parity principle.[37]

80. Slovenia retorts that the "Law on the Fund for Financing the Decommissioning of the Krško Nuclear Power Plant and the Disposal of Radioactive Waste of the Krško Nuclear Power Plant" was a necessary measure in order for it to comply with its international obligations as a nuclear State:[38]

> In the eyes of the international community as a result of its status as a nuclear State, it would ultimately be responsible for the costs of the process of the decommissioning of the Krško NPP.[39]

Since Slovenia was internationally responsible for the decommissioning costs, it was compelled to ensure that these responsibilities were met by the creation of the Decommissioning Fund.[40] The Krško NPP was liable for payments to the Decommissioning Fund on a monthly basis, collected by NEK by means of a surcharge factored into the selling price of the electricity produced by Krško NPP. The intention was that an equal amount would be charged to both HEP and ELES, in accordance with the parity principle, and that contributions collected from the buyer from each State would be credited towards that State's 50% share of the total cost of decommissioning.[41]

81. NEK was liable to make payments to the Decommissioning Fund, regardless of whether it had itself received contributory payments from its buyers. Croatia would not pay its share of the decommissioning costs.[42]

The Replacement of the Steam Generators at the Krško NPP

82. On 10 February 1995 the Management Board decided on the replacement of the steam generators.[43] In September 1995 the Government of Slovenia issued a "Decision"

[36] Claimant's Memorial, para 81

[37] Claimant's Memorial, para 83

[38] Respondent's Counter-Memorial, para 80

[39] Respondent's Counter-Memorial, para 79

[40] Respondent's Counter-Memorial, para 82

[41] Respondent's Counter-Memorial, para 83

[42] Respondent's Counter-Memorial, para 84

[43] Claimant's Memorial, para 90; Respondent's Counter-Memorial, para 60

supporting a modernisation programme. In Paragraph 4 of that Decision the Government of Slovenia announced that:[44]

> In the preparation and realization of the renovation of the NPP Krško NPP, the Nuclear Power Plant Krško shall act in the capacity of the investor.

83. According to HEP, Mr Rožman, the General Manager of NEK and a Slovenian national, based on the Government of Slovenia's September 1995 Decision ignored the decision of NEK's Management Board which mandated a team of two Croatian and two Slovenian representatives to supervise the steam generator replacement project. NEK proceeded on its own with respect to the plant modernisation programme.[45] Mr Rožman invited HEP to presentations on the progress of the steam generator replacement programme, but did not form an Operational Team to manage the modernisation process, as a 1995 Krško Board directive requested.[46]

84. Slovenia contends that Croatia proposed Mr Vrankić and Mr Udovicic as HEP's nominees to the Operational Team, whereas Slovenia did not make any nominations. Instead, according to the September 1995 Government Decision, it delegated all competences connected with the modernisation project to NEK. Thus, two employees of NEK, Messrs Rožman and Novsak, were delegated as Slovenia's representatives. When Mr Rožman attended the modernisation project Operational Team meeting on 7 June 1996 on behalf of Slovenia, HEP declined to acknowledge the competence of Slovenia's representatives.[47]

<u>The Dispute on the Appointment of NEK's Deputy General Manager</u>

85. The 1982 Self-Management Agreement provided that the incorporators from Croatia were to appoint the Deputy General Manager of NEK. In February 1996 the Deputy General Manager of NEK resigned. By letter dated 4 September 1996, addressed to Mr Rožman, HEP nominated Mr Vrankić as Deputy General Manager. Mr Rožman rejected this appointment. He noted in his letter of 30 September that the Self-Management Agreement had become inadequate in the section concerning personnel,[48] that personnel decisions should be based on "safety, stability and operational efficiency", and that candidates for managerial positions had to be qualified in the fields of nuclear technology and safe operation of power plants, which qualifications Mr Vrankić lacked.[49]

86. In response to continuing differences between the Croatian and Slovenian members of the NEK Management Board, the Government of Slovenia created by means of a Decision of 15 May 1997 a "Temporary Management Board", consisting of four members nominated by each founder, to oversee NEK.[50] Slovenia argues that the

[44] Exhibit C-41

[45] Claimant's Memorial, paras 93 *et seq.*

[46] Claimant's Memorial, para 101

[47] Respondent's Counter-Memorial, para 62

[48] Exhibit C-52

[49] Claimant's Memorial, paras 107 *et seq.*

[50] Exhibit C-71; Claimant's Memorial, para 112

Temporary Management Board was created later, in September 1997, by an agreement of Minister Porges of Croatia and Minister Dragonja of Slovenia in Portorož.[51]

87. In a letter dated 9 February 1998, the Slovenian Ministry of Economic Affairs informed the Chairman of NEK's Temporary Management Board that it agreed to the appointment of Mr Vrankić.[52] The Temporary Management Board authorised Mr Rožman to appoint Mr Vrankić as Deputy General Manager. Mr Rožman, however, refused, claiming that Mr Vrankić did not possess the necessary qualifications (for example, a Senior Reactor Operator Licence ("SRO licence")).[53]

88. At a meeting of the Temporary Management Board on 24 April 1998, HEP withdrew its consent to the nomination of Mr Rožman as General Manager of NEK and declared that it would only resume its participation on the Temporary Management Board once Mr Vrankić was installed as Deputy General Manager. At the same meeting HEP declared that since Mr Vrankić had not been appointed Deputy General Manager, after 15 March 1998 HEP would not pay for the electricity it took from the Krško NPP.[54]

89. Slovenia insists on the fact that the only reason why Mr Rožman was not eager to accept Mr Vrankić's appointment was because the latter lacked the necessary qualifications.[55] Mr Rožman's point was not that HEP did not have the right to nominate NEK personnel, "only that such right was constrained by overarching safety imperatives."[56] Neither the Temporary Management Board nor Mr Rožman were competent to waive mandatory conditions set out in NEK's Safety Analysis Report ("SAR") or NEK's operating licence.[57] Slovenia highlights that the Krško NPP Safety Committee ("KSC") opposed Mr Vrankić's appointment.[58]

90. HEP denies that the reason behind Mr Rožman's refusal to appoint Mr Vrankić as Deputy General Manager was the absence of an SRO licence. HEP stresses that: (i) NEK has had three Deputy General Managers who did not have SRO licences; (ii) Mr Rožman based his rejection in his letter of 30 September 1996 primarily on the grounds that the Governing Agreements were no longer adequate; and (iii) in February and April 1998 the Government of Slovenia eventually consented to Mr Vrankić's appointment, even though he did not have the SRO licence.[59]

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[51] Exhibit C-83; Respondent's Counter-Memorial, para 42

[52] Claimant's Memorial, para 114

[53] Claimant's Memorial, para 116

[54] Respondent's Counter-Memorial, para 55

[55] Respondent's Counter-Memorial, para 50

[56] Respondent's Counter-Memorial, para 52

[57] Respondent's Counter-Memorial, para 53

[58] Respondent's Counter-Memorial, para 53

[59] Claimant's Reply Memorial on the Merits ("Claimant's Reply"), para 84

The Dispute over HEP's Financial Obligations towards the Krško NPP

91. Slovenia emphasises that NEK operates the Krško NPP on a cost-covering basis. NEK's sole source of revenue came from selling the electricity produced by the plant. Slovenia states that Croatia used to make delayed and incomplete payments for electricity it received during the nineties, which lead to NEK suffering crippling debts. NEK's annual profit and loss account for 1998 showed a total net loss in the amount of Slovenian tolars (SIT) 5,752 million.[60]

92. According to Slovenia, the following table shows the respective debts of HEP and ELES towards NEK in the period 1996-1998:

	31 December 1996		31 December 1997		30 June 1998	
	HEP	ELES	HEP	ELES	HEP	ELES
Total Debt to NEK in million SIT	9,023	923.8	17,703.2	(credit: 96.9)	16,689.5	844.4

93. Slovenia's calculation also reflects the sums owed by NEK to ELES for pooled depreciation assets. NEK had paid to HEP its share of these resources (by 1997, NEK had paid HEP over USD 175.7 million as pooled depreciation funds)[61] but not to ELES.[62] Slovenia stresses that HEP did not pay its part of the decommissioning costs[63] and of the costs for the modernisation of Krško NPP.[64]

94. On 13 September 1997 an agreement was signed in Portorož between the Croatian Minister of Economy, Mr Nenad Porges and the Slovenian Minister of Economic Affairs, Mr Metod Dragonja, according to which agreement the price of electricity would be calculated "ex plant" for both buyers. Pursuant to that agreement, decommissioning costs would not be included in the price of electricity, as each State would regulate independently its share of the costs pending the execution of a new bilateral agreement that would govern cooperation between the two States including decommissioning of the Krško NPP.[65]

95. It was agreed that within a month, the Croatian side would provide a guarantee for coverage of its share of decommissioning costs. According to Slovenia no such

[60] Respondent's Counter-Memorial, paras 88-89

[61] Exhibit R-37, p 4

[62] Respondent's Counter-Memorial, paras 90, 91

[63] Respondent's Counter-Memorial, paras 96 *et seq.*

[64] Respondent's Counter-Memorial, paras 100 *et seq.*

[65] Respondent's Counter-Memorial, para 98

guarantee was provided.[66] HEP disagrees. According to HEP, Croatia did provide such a guarantee, even though it delayed doing so by approximately five months.[67]

96. Following the Portorož Agreement, invoices sent to HEP continued to include decommissioning charges. Slovenia notes that these charges were calculated separately from the cost elements, and NEK only pressed HEP to pay the electricity price, and not the decommissioning cost.[68]

97. HEP would not pay the amount as established in NEK's invoices. HEP insisted that it would pay US2.05 cents per KWh, even though, according to Slovenia, the actual operating costs in 1997 indicated a price of US3.0841 cents per KWh (not including decommissioning costs).[69] Slovenia states that despite several meetings between the ministers of Croatia and Slovenia, HEP continued to make only partial payments, and even stopped paying for electricity altogether as of 15 March 1998.[70]

98. HEP argues that Croatia's refusal to meet its decommissioning obligations prior to 1998 has nothing to do with the disputed issues in the case. Any such dispute should be solved according to the dispute resolution provisions of the 2001 Agreement.[71]

99. HEP refers to the witness statement of Damir Begović and explains how it calculated the cost of electricity at US2.05 cents per KWh.[72] It also denies that it stopped making any payments as of March 1998. It mentions that during the months of March to December 1998 it paid to NEK approximately US$27.2 million.[73] Moreover, according to HEP, the calculation of HEP's debt to NEK by Slovenia is false, for the following reasons:

- It includes the decommissioning costs, even though it had been agreed in Portorož that NEK would not request HEP to pay these charges.[74]

- One of the reasons as to why HEP's financial obligations towards NEK appeared to be more extended than the Slovenian investor's, ELES's, obligations, is a result of the Slovenian accounting regulations. HEP claims that it serviced the loans originally obtained by its predecessor Croatian electric companies to fund their initial US$600 million investment in the Krško NPP completely independently of NEK. Slovenian loans on the other hand were transferred to NEK's books from 1986 onwards, and the debt service was paid after that by NEK on behalf of ELES.[75]

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[66] Respondent's Counter-Memorial, para 98

[67] Claimant's Reply, para 11

[68] Respondent's Counter-Memorial, para 99

[69] Respondent's Counter-Memorial, para 109

[70] Respondent's Counter-Memorial, paras 114 *et seq.*

[71] Claimant's Reply, para 10

[72] Claimant's Reply, para 109

[73] Claimant's Reply, para 113

[74] Claimant's Reply, paras 92 *et seq.*

[75] Claimant's Reply, para 79

- The calculation ought not to include the credit due from NEK to the incorporators for pooled depreciation assets.[76]

100. Had the above not been taken into account, HEP's debt to NEK in 1998 would amount to 3,132 millions SIT, whereas ELES's debt would be 2,683 million SIT.[77] Slovenia disagrees with HEP's calculation of its debts to NEK.[78] It considers for example that HEP cannot subtract the decommissioning costs from its own debts but include them in its calculation of ELES's debts to NEK.[79] The same is argued for the depreciation costs.[80]

NEK's Financial Problems

101. Slovenia states that the non-payment by HEP brought NEK to the brink of operational shutdown.[81] NEK was effectively insolvent in mid-1998: it lacked the funds to pay for nuclear fuel and the employees' salaries, or to carry out the necessary maintenance.[82]

102. HEP responds that Slovenia's description of NEK's finances in July 1998 is exaggerated: (i) NEK did not start to have financial problems in 1998. Rather, NEK had suffered chronic liquidity problems since 1993;[83] (ii) HEP's debts to NEK are exaggerated, and the bulk of HEP's debts was disputed and had no impact on NEK's then current business operations (for example, the "decommissioning debts" to NEK was a charge to finance future expenditures, and therefore had no current impact on the operation of the Krško Plant during the years 1996-1998);[84] (iii) the ELES GEN debts to NEK contributed significantly to the chronic liquidity problems at the Krško NPP;[85] and (iv) the gravity of NEK's financial condition in 1998 is exaggerated (for example, the reports to which Slovenia refers do not support Slovenia's proposition that "NEK had been effectively insolvent for over three years").[86]

103. Slovenia disagrees with all of the above. It stresses, for example, that, in order to be able to finance the eventual decommissioning of the Krško NPP, funds had to be collected well in advance.[87]

[76] Claimant's Reply, para 94

[77] Claimant's Reply, paras 95-96

[78] Slovenia's Rejoinder ("Respondent's Rejoinder"), paras 61 *et seq.*

[79] Respondent's Rejoinder, para 65

[80] Respondent's Rejoinder, para 66

[81] Respondent's Counter-Memorial, para 126

[82] Respondent's Counter-Memorial, paras 135 *et seq.*

[83] Claimant's Reply, paras 87 *et seq.*

[84] Claimant's Reply, paras 90 *et seq.*

[85] Claimant's Reply, para 97

[86] Claimant's Reply, paras 98 *et seq.*

[87] Respondent's Rejoinder, para 78

The Nuclear Safety Concerns at the Krško NPP

104. Slovenia highlights that, as a result of HEP's non-payment for the deliveries of electricity, NEK did not have the necessary funds to secure its safe operation and had to seek alternative buyers for the electricity.[88] HEP counters that Croatia's capital, Zagreb, is located only 40 km downstream from the Krško NPP, so the proposition that HEP was disinterested in safety is incorrect.[89]

105. Moreover, HEP asserts that the SNSA (the nuclear agency of the Republic of Slovenia) reports dealing with the Krško NPP that were produced by Slovenia in discovery do not support the assertion that the financial condition of NEK had created any threat to the safe operations of the Krško NPP.[90] According to HEP, reports of different agencies and bodies prior to 1998 (some of which were referred to by Slovenia) do not support this conclusion either.[91] Similarly, there is no report subsequent to 1998 which would support the assertion that the Krško Plant had any nuclear safety problems.[92]

106. Slovenia denies HEP's interpretation.[93] It notes that the reports were written in such a way so as not to cause undue public alarm,[94] and that, contrary to HEP's submissions, most of the reports stated that the steam generators should be replaced.[95] It also notes that the reports reflect concerns about NEK's financial situation.[96]

The Suspension of Electricity Deliveries to HEP

107. On 30 July 1998 NEK suspended its electricity deliveries to HEP.

108. HEP argues that the two 400 kV transmission lines over which electricity had been delivered from the Krško NPP to HEP were disconnected.[97] HEP argues that the decision to disconnect these transmission lines was made by: 1) Mr Metod Dragonja, the Minister of Economic Affairs for the Republic of Slovenia; 2) Dr Banič, the General Manager of ELES and the Slovenia-appointed Chairman of the Temporary Management Board of NEK; and 3) Mr Rožman, the General Manager of NEK.[98]

109. HEP notes that Slovenia cannot use HEP's alleged failure to pay for electricity as an excuse for taking this measure. Clause 6.1 of the 1974 Pooling Agreement and the 1982 Annex to the Pooling Agreement provided that the co-owners of the Krško NPP

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[88] Respondent's Counter-Memorial, paras 8, 143 *et seq.*

[89] Claimant's Reply, paras 4, 57

[90] Claimant's Reply, paras 118 *et seq.*

[91] Claimant's Reply, paras 126 *et seq.*

[92] Claimant's Reply, paras 153 *et seq.*

[93] Respondent's Rejoinder, paras 81 *et seq.*

[94] Respondent's Rejoinder, para 84

[95] Respondent's Rejoinder, para 88

[96] Respondent's Rejoinder, paras 91 *et seq.*

[97] Claimant's Memorial, para 126

[98] Exhibit C-21; Claimant's Memorial, para 127

cross-guaranteed each other's financial obligations.[99] Further, HEP stresses that the Governing Agreements provided for the resolution of any disputes by arbitration, and not by unilateral action.[100]

110. HEP refers to a comment made by the Slovenian Minister for Spatial Planning and the Environment, Mr Janez Kopač, during a 2002 television appearance in which he concluded that HEP's exclusion from the Krško NPP amounted to a theft.

111. Slovenia disagrees, and by contrast highlights that the reason why the electricity deliveries to HEP were suspended was because HEP would not pay for the deliveries of electricity. As a consequence, NEK did not have the necessary funds to secure its safe operation and had to seek alternative buyers for the electricity.[101] Irrespective of the above, Slovenia disagrees with HEP's interpretation of Clause 6.1 of the 1974 Pooling Agreement and the 1982 Annex to the Pooling Agreement and denies that it provided for a cross-guarantee of the parties' financial obligations.

112. Slovenia also emphasises that the termination of electricity supply to HEP was intended to be a strictly temporary measure. This is evidenced by the fact that the electricity not delivered to HEP was sold on the short-term "spot" market.[102]

In its Rejoinder, Slovenia notes that:[103]

> [t]here is a distinction to be drawn between physical flows of electricity and how that electricity is purchased. A person may physically acquire electricity from persons other than from persons with whom it contracts to purchase it. Contracts may change, but the physical flows do not. The Tribunal should not be under any misapprehension that HEP or Croatia were deprived of actual energy flows from the Krško NPP. In fact, apart from a very brief period 10 years ago – just a few days – there was no physical cut-off at all. Even then, only two of the several transmission lines from Slovenia to Croatia were affected. Beyond this, throughout the whole of the relevant period Croatia continued to receive electricity from the Krško NPP in exactly the same way as it had done before July 1998 and indeed does so today. Zagreb continued to be powered by the electricity of the Krško NPP. Rather than any physical termination of electricity supply, what occurred is merely that on the contractual plane (i.e. as a matter of accounting or booking entries) as opposed to the physical plane, over this period HEP was deemed to have to purchase that electricity from other sources. All that HEP lost in July 1998 was the contractual ability to claim electricity from the Krško NPP. Indeed, this is all it seeks compensation for in damages.

Slovenia's Proposals For an Agreement Over Electricity Supply to HEP

113. In late October 1998 Slovenia proposed conditions for an agreement for the resumed delivery of electricity from the Krško NPP to both HEP and ELES.[104] The proposal included an offer of electricity at the same price to both ELES and HEP.

[99] Claimant's Memorial, para 135

[100] Claimant's Memorial, paras 136 *et seq.*

[101] Respondent's Counter-Memorial, paras 8, 143 *et seq.*

[102] Respondent's Counter-Memorial, para 146

[103] Respondent's Rejoinder, para 10

[104] Exhibit C-157

Decommissioning costs were excluded from the offered price. Croatia rejected this proposal on 10 November 1998. The Croatian Minister Porges complained in his letter sent to the Slovenian Minister, Mr Dragonja, that accepting the offer would put HEP in the position of a buyer. He also complained that the proposed production expenses were too high and not competitive.[105]

114. In January 2000 Slovenia made another offer to restore the electricity supply to HEP for a period of two years.[106] HEP rejected this offer, considering the price to be too high.[107]

The 1998 Decree

115. On 31 July 1998, the Slovenian Government published a "Decree on Transformation of Nuklearna Elektrarna Krško po into Javno poduzeće Nuclearna Elektrarna Krško d.o.o." (the "1998 Decree").[108] The 1998 Decree stipulated that it would remain applicable until the entry into force of a bilateral agreement between the Republic of Slovenia and the Republic of Croatia.

116. HEP claims that several provisions of the 1998 Decree violate the Governing Agreements:[109]

- Article 1 stipulated that, pending execution of "the appropriate bilateral agreement between the Republic of Slovenia and the Republic of Croatia", the incorporator's rights in Javno poduzeće Nuklearna elektrarna Krško, a limited liability company (transformed by the Decree of the Government of the Republic of Slovenia of July 30, 1998 from Nuklearna elektrana Krško p.o.) ("JP NEK") were to be exercised by the Government of Slovenia;

- Article 6 granted HEP the right to participate in the management of JP NEK, taking into account the Governing Agreements, "unless the same is contrary to this Decree";

- By virtue of Articles 20 and 21, JP NEK's Management Board consisted of eight members, four appointed by Slovenia and four by Croatia. In the event of a tie vote in respect of any decision of the Management Board, the Slovenia-appointed Chairman would have a controlling vote;

- Article 23 granted primary management responsibility to a manager, who was to be appointed by Slovenia;

- Article 16 authorised JP NEK not to deliver electricity to HEP in the event that its outstanding obligations exceeded the value of two-months' delivered electricity;

[105] Respondent's Counter-Memorial, para 235

[106] Exhibit C-170

[107] Exhibit C-171; Respondent's Counter-Memorial, para 236

[108] Exhibit C-137

[109] Claimant's Memorial, paras 132, 133

- Article 30 stated that if an agreement on the price of electricity was not reached between JP NEK, ELES and HEP "within 60 days from the date of entry into force hereof, the price and terms of delivery of electricity should be determined by the incorporator", *i.e.* by the Slovenian Government. This violated HEP's right to participate in all decisions affecting the price of electricity produced at the Krško NPP;[110] and

- Article 34 required that NEK's claims against HEP with respect to "pooled depreciation resources" were to be set off against HEP's investment in the Krško NPP, thus, according to Croatia, diluting HEP's overall percentage of ownership of the plant.

117. HEP stresses that the reason behind the enactment of the 1998 Decree cannot be NEK's crippling financial situation and concerns about nuclear safety, since Slovenia had been planning the 1998 Decree for at least eighteen months.[111] Slovenia responds that, after Slovenia's independence in 1991, NEK remained a work organization pursuant to the old Yugoslav system of associated labour. NEK was required to restructure itself in line with the Law on Commercial Companies by 31 December 1994 at the latest. Since this did not happen, from 1 January 1995 NEK risked being liquidated by the Slovenian courts. NEK was also obliged to transform its socially-owned capital to "known" ownership by 1 August 1998. Otherwise, its capital would have become property of the Development Corporation of Slovenia.[112]

118. Soon after their independence, Slovenia and Croatia started discussions regarding the need for a new bilateral agreement governing their relations in connection with the Krško NPP. The reorganisation of NEK in line with Slovenia's new company laws was postponed in the hope that negotiations would bring about a new bilateral agreement that would resolve NEK's status.[113] In 1998, since NEK's financial position was dire, and since no progress had been achieved towards a bilateral agreement, Slovenia submits that it was forced to enact the 1998 Decree.[114]

119. NEK, therefore, had to be restructured. From Slovenia's perspective, there was no possibility of restructuring NEK by means of an agreement with HEP, since the latter was obstructing NEK's management. For example, HEP "refused to cooperate with management processes," which resulted in no further meetings of the Board of Directors being held between 7 June 1996 and May 1997. Even after the Portorož Agreement, where the rules of procedure for the new Temporary Management Board were adopted, HEP continued obstructing decision-making.[115]

120. As to the content of the 1998 Decree, Slovenia stresses that it preserved HEP's interests. First of all, it did not deprive HEP of any ownership rights in the Krško

[110] Claimant's Reply, paras 65 *et seq.*

[111] Claimant's Reply, para 165

[112] Respondent's Counter-Memorial, paras 149-151, 159-160; Slovenia submits no documentary evidence in support of this last assertion.

[113] Respondent's Counter-Memorial, para 147

[114] Respondent's Counter-Memorial, para 147

[115] Respondent's Counter-Memorial, para 155

NPP, since HEP did not have any ownership rights until the entry into force of the 2001 Agreement, on 11 March 2003.[116] Furthermore, the 1998 Decree expressly recognised and preserved the rights and invested assets of the Croatian co-founder. For example, Article 1 states:

> The Republic of Croatia, *ie* Hrvatska Elektroprivreda dd Zagreb, which is the holder of rights and liabilities under this Decree, is recognised as the co-investor under this Decree based on invested assets (pooled resources).

Any adjustments to the value of assets held by either party would only be provisional and would be subject to settlement by the new bilateral agreement.[117]

121. Slovenia also argues that the 1998 Decree did not block HEP's participation in the management and operation of the Krško NPP, or the parity principle. The existing Temporary Management Board of NEK was retained and renamed the New Management Board. The arrangement in the Governing Agreements, whereby the chairman of the Management Board and the manager of NEK were to be appointed by the Slovenian party was retained. Only in order to guard against "deadlock" would the vote of the chairman prevail. Slovenia stresses that this arrangement was never invoked, although it was replicated by Slovenia and Croatia in the 2001 Agreement.[118]

122. On 31 December 1999 HEP commenced proceedings before the Slovenian Constitutional Court claiming that the 1998 Decree was unconstitutional and contrary to the Energy Charter Treaty.[119] HEP's application was dismissed on 15 May 2003 on the basis that the 1998 Decree has been a temporary measure. The Constitutional Court held that when the 2001 Agreement entered into force on 11 March 2003 "the initiator lost the legitimate interest for the evaluation of compliance of the Decree with the Constitution."[120]

THE 2001 AGREEMENT

<u>Negotiations Leading to the 2001 Agreement</u>

123. Several meetings between Slovenian and Croatian Ministers on the issue of Krško NPP took place after August 1998. A breakthrough in the parties' negotiations came at a meeting of the Croatian and Slovenian Prime Ministers at Rijeka held in June of 2001, on the basis of the proposal of Dr Granić, the Deputy Prime Minister of Croatia. The proposal for an agreement was made along the following lines: (i) all sums claimed by each side would be waived; (ii) HEP would be recognised as co-owner and co-manager of Krško NPP; and (iii) the delivery of electricity to HEP from Krško NPP would be resumed as of an agreed date.[121]

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[116] Respondent's Counter-Memorial, para 167

[117] Article 7, 1998 Decree; Respondent's Counter-Memorial, para 170

[118] Respondent's Counter-Memorial, para 175

[119] Respondent's Counter-Memorial, para 277

[120] Respondent's Counter-Memorial, para 279

[121] Claimant's Memorial, paras 148-151

124. An issue that had to be decided during the negotiations was the date(s) as of which the waiver of the financial claims and the resumption of electricity deliveries would take place. HEP submits that this agreed date was 30 June 2002. It alleges that in the meeting in Rijeka the Croatian proposal was to select 1 January 2002 as the key date. Slovenia suggested 30 June 2002.[122] Croatia states that:

> [t]he bargain stuck between the Prime Ministers of the two countries at Rijeka on June 9, 2001, had as its centre a simple *quid pro quo*: Croatia and HEP waived all financial claims against Slovenia, ELES and NEK up to, but not beyond June 30, 2002; in return, Slovenia agreed that the Krško NPP would resume delivery of 50% of its power output to HEP on that date. Without such a *quid pro quo*, Croatia would not have entered into the 2001 Agreement.

125. Slovenia criticizes this *quid pro quo* as an oversimplified explanation of the settlement reached between the two States. More specifically, Slovenia claims that the above view disregards the fact that, in return for Croatia agreeing to waive its financial claims, Slovenia also waived its past claims for the non-payment by Croatia of its financial obligations towards NEK.[123]

126. HEP emphasises that at a meeting on 28-30 June 2001 at Brijuni (Brioni), Croatia, the draft for an agreement on the resumption of electricity deliveries of both sides, Croatian and Slovenian, contained the date of 30 June 2002. The Croatian draft read:

> The shareholder from the Republic of Slovenia shall receive all generated power and electricity and financial effects related to the production thereof for the period from August 1, 1998 until the date on which HEP d.d. starts receiving electricity again, which means until June 30, 2002.

The Slovenian drafted read:[124]

> The Slovenian shareholder shall take all the generated power and electricity and any financial effects associated with the production thereof for the period from August 1, 1998 until the date of the receiving of electricity by HEP d.d., but not later than by June 30, 2002.

127. Both parties agree that the attendees at the meeting at Rijeka and at Brijuni (Brioni) expected that the agreement between the two States would be signed by mid-July 2001 and ratified by the end of 2001.[125] Slovenia argues that the 30 June 2002 date meant that the parties agreed that their financial relations would be balanced as of six months from the expected date of entry into force of the Agreement.[126]

The Content of the 2001 Agreement

128. The 2001 Agreement was signed on 19 December 2001 by the Croatian Minister of Economy, Mr Goranko Fižulić, and by the Slovenian Minister of Environment and Planning, Mr Kopač. The recitals state that the two Governments took into account the Governing Agreements in agreeing upon the terms of the 2001 Agreement. They

[122] Claimant's Memorial, para 156; this statement is supported by witness evidence, not contemporaneous documentary evidence.

[123] Respondent's Counter-Memorial, para 211

[124] Claimant's Memorial, para 163

[125] Claimant's Memorial, para 157; Respondent's Counter-Memorial para 206

[126] Respondent's Counter-Memorial, para 206

also state that the 2001 Agreement is based on the Energy Charter Treaty, the Convention on Nuclear Safety, and the Joint Convention on the Safety of Spent Fuel Management and on the Safety of Radioactive Waste Management.

129. The 2001 Agreement:

- recognizes HEP and ELES-GEN as the legal successors in interest to the Slovenian and Croatian companies that invested in the construction of Krško NPP;[127]

- provides that HEP and ELES-GEN shall have equal rights and obligations, unless otherwise stated in the Agreement;[128]

- establishes HEP and ELES-GEN as 50:50 shareholders in the limited liability company NEK d.o.o., a new legal entity to be governed by a Memorandum of Association (Exhibit 1 to the 2001 Agreement. The Memorandum of Association states in Article 2 that the transformation of NEK will take place in accordance with the 2001 Agreement and Slovenian company law. It also provides in Article 30 that NEK may terminate electricity deliveries to either shareholder if that shareholder fails to comply with its financial obligations.);[129]

- states that the governance of NEK d.o.o. will be exercised in accordance with the parity principle. ELES-GEN nominates the Chairman of the Management Board and HEP the Vice-Chairman. HEP nominates the Chairman of the Supervisory Board and ELES-GEN the Vice-Chairman. The Chairman of the Management Board has a casting vote, which vote is to be controlled by the Supervisory Board;[130]

- orders that electricity produced at the Krško NPP shall be delivered to the shareholders in equal proportions;[131]

- states that the price for electricity deliveries comprises operating costs in the amounts necessary for long-term investment, and includes, *inter alia*, the depreciation costs;

- stipulates that decommissioning and radioactive waste disposal are joint liabilities of Croatia and Slovenia and shall be financed in equal proportions. The funds for decommissioning shall be collected in a special fund created by each State;[132]

- Concerning the past financial issues, Article 17 of the 2001 Agreement provides that:

[127] Article 1(a), 2001 Agreement

[128] Article 1(b), 2001 Agreement

[129] Article 2, 2001 Agreement

[130] Article 3, 2001 Agreement

[131] Article 5, 2001 Agreement

[132] Articles 10 and 11, 2001 Agreement

Past Financial Issues

(1) Mutual financial relations existing up to the signing of this Agreement between NEK d.o.o., ELES d.o.o., and HEP d.d. shall be regulated in accordance with the principles set forth in Exhibit 3 of this Agreement.

(2) The Contracting Parties agree that, as of the date of entry into force hereof, all obligations of NEK d.o.o. to the Fund for financing the dismantling of NE Krško and disposal of radioactive waste from NE Krško, which obligations arose from the application of the Act on Fund for Financing of Dismantling of NE Krško and Disposal of Radioactive Waste from NE Krško... shall cease to exist.

130. Article 19 contains the dispute resolution provision. Article 19(2) reads:

> If a dispute cannot be settled amicably within six months from the date of written report to the other Contracting Party, the aggrieved Shareholder may, at its discretion, refer the dispute for resolution to: ... e) the International Centre for Settlement of Investment Disputes – ICSID – in accordance with the Convention on the Settlement of Investment Disputes between States and Nationals of Other States and the additional contract on regulation of Conciliation, Arbitration and Fact-finding.

131. Article 22 of the 2001 Agreement ("Closing Provisions") stipulates that:

> By entry into force of this Agreement, the provisions of the [1970 Agreement] shall cease to have effect.
>
> All other issues which are not stipulated herein shall be governed by the Agreement between the Government of the Republic of Croatia and the Government of the Republic of Slovenia on stimulation and mutual protection of investments. This Agreement shall be ratified by the Croatian Parliament, i.e. in the Parliament of the Republic of Slovenia.
>
> This Agreement shall enter into force on the date of receipt of the last written diplomatic notice that all conditions as required by the legislations of the Contracting Parties required for its entry into force have been complied with.

132. Exhibit 3 of the 2001 Agreement, to which reference was made in Article 17 (see the last bullet point in Paragraph 148, above), regulates the past financial issues between the Parties:

> PRINCIPLES OF THE STRUCTURING OF THE FINANCIAL RELATIONS
>
> (1) ELES GEN d.o.o. shall assume all obligations of NEK d.o.o towards the bank which have occurred as a result of the transfer to NEK d.o.o of the repayment of investment loans made by the Slovene founders, according to the balance on December 31, 2001. Obligations resulting from loans issued to carry out NEK's modernization project will be NEK d.o.o's only remaining long-term financial obligations. Until June 30, 2002, the cost of these loans will be borne through the cost of electricity by the Shareholder from the Republic of Slovenia and from that day forward by both Shareholders.
>
> (2) By virtue of the entry into force of this Agreement:
>
> -HEP d.d. waives all claims against NEK d.o.o for damages, i.e. for compensation for undelivered electricity, i.e. for compensation for use of the capital, and in this regard will fully waive all claims in court arising therefrom;

-NEK d.o.o waives all claims against HEP d.d. in connection with delivered power and electricity, and in this regard will fully waive all claims in court arising therefrom;

-NEK d.o.o waives its claims against ELES d.o.o in the same amount as in the previous bullet of this Paragraph;

-NEK d.o.o. waives all claims against HEP d.d. in connection with charged fees for financing of the dismantling of the Nuclear Power Plant Krško and disposal of radioactive waste from Nuclear Power Plant Krško, and in this regard will fully waive any claims in court arising therefrom;

-NEK d.o.o. waives all claims in connection with pooled resources of depreciation of both founders and claims in connection with the coverage of losses from previous years.

(3) Based on the provisions listed above, NEK d.o.o will rearrange its balance sheet on December 31, 2001 so that:

-it shows neither any claims torward HEP d.d. and ELES d.o.o nor any obligations toward the fund for financing of the dismantling of the Nuclear Power Plant Krško and the disposal of radioactive waste from the Nuclear Power Plant Krško;

-it does not show any obligations toward the bank which occurred as a result of the transfer of repayment of Slovene founders' investment loans to NEK d.o.o. described in Paragraph 1 of this Exhibit;

-based on the conversion of HEP's long term investments and the exemption of the loan, NEK d.o.o's capital will, after the payment of the possible uncovered losses, be distributed to the Shareholders in two equal parts, so that the initial capital of NEK d.o.o. reaches the amount listed in Article 2 of this Agreement, and so that any possible remainder is distributed into the reserves;

-any other necessary accounting corrections or changes arising from this Exhibit are executed.

(4) Any possible profit to NEK d.o.o. arising from accounting corrections or changes described in Paragraph 3 of this Exhibit will be tax-exempt.

(5) ELES GEN d.o.o assumes the financial results of all power and electricity produced during the period from July 31, 1998 until the date HEP d.d. begins to take over the electricity again, but no later than June 30, 2002. All the while, NEK d.o.o.'s financial position must not worsen compared to its financial position on July 30, 1998.

(6) The Contracting Parties will ensure that the Shareholders determine, by no later than the end of 2002, whether the company needs additional long-term sources of financing its operating costs, which sources of financing will be secured by a capital increase in NEK d.o.o. or any other appropriate manner.

133. HEP submits that the agreed deadline between the parties for the restoration of electricity deliveries to HEP,[133] as well as the deadline for the waiver of its financial claims against NEK, was 30 June 2002.[134]

134. Slovenia disagrees. It denies that Exhibit 3 contains an express obligation to supply HEP with electricity on 30 June 2002. It points out that the only provision in the 2001 Agreement for restoration of actual electricity deliveries is its Article 5(2):

[133] Article 5, Exhibit 3 to the 2001 Agreement

[134] Article 2, Exhibit 3 to the 2001 Agreement

> (2) The Contracting Parties agree that the Company shall deliver the produced power and electricity to the Shareholders in equal proportions, half to each Shareholder, until the end of the regular useful life of the nuclear power plant in the year 2023, i.e. until the extended useful life of the power plant, if approved (hereinafter: useful life).

Slovenia stresses that Exhibit 3 did not deal with the electricity supply to HEP, but with the terms of the financial settlement. It notes that Exhibit 3 is entitled "Principles of the Restructuring of the Financial Relations", and that the agreement of the parties was that a financial equilibrium between the parties should be deemed to have been reached as of six months after the date of entry into force of the agreement.[135]

135. Slovenia also contends that it was only with the entry into force of the 2001 Agreement that HEP's rights in relation to Slovenia were activated, and that this is confirmed by the heading of Exhibit 3's Paragraph (2): "By virtue of the entry into force of this Agreement."[136]

The Ratification of the 2001 Agreement

136. The initial idea of the negotiating parties was that the 2001 Agreement would be ratified by Slovenia and Croatia by the end of 2001.[137] The Governments of Croatia and Slovenia issued a Joint Statement on 19 December 2001, when the 2001 Agreement was signed, announcing that they should use their best efforts to achieve the ratification of the 2001 Agreement "as soon as possible during the first quarter of 2002".[138]

137. In fact, however, Croatia ratified the 2001 Agreement on 3 July 2002 and Slovenia ratified the 2001 Agreement on 25 February 2003,[139] following unsuccessful litigation attacking its constitutionality. In Slovenia the signature and ratification of the 2001 Agreement had met with parliamentary and public opposition for a long time.[140] On 10 March 2003 the Slovenian Foreign Ministry advised Croatia of Slovenia's ratification. Croatia received the diplomatic notice on 11 March 2003.[141]

138. The resumption of electricity deliveries of Krško-generated electricity to HEP took place on 19 April 2003.

NEK's Offers For Sale of Electricity

139. On 24 June 2002 NEK had sent HEP an offer for the supply of electricity during the six month period 1 July 2002 – 31 December 2002 (the "June 2002 Offer"). Slovenia

[135] Respondent's Counter-Memorial, para 206

[136] Respondent's Counter-Memorial, paras 211, 212

[137] Claimant's Memorial, para 157; Respondent's Counter-Memorial, para 206

[138] Claimant's Memorial, paras 281 *et seq.*

[139] Claimant's Memorial, paras 178-181

[140] Respondent's Counter-Memorial, paras 22 *et seq.*

[141] Respondent's Counter-Memorial, para 233

states that the fact that the 2001 Agreement would not come into force by 30 June 2002 caused concerns within Slovenia because:[142]

> it meant that the deemed financial equilibrium expected to occur on 30 June 2002 would not happen, and nor would HEP begin to receive electricity again. The ramifications were unclear to the Slovenian Government. [...] Understandably, (although, as it turns out, mistakenly), Slovenia assumed that if it offered to supply electricity to HEP, even if this was done outside the framework of the still-to-be-ratified 2001 Agreement, that this would eliminate any risk that Croatia or HEP would bring a damages claim against Slovenia or NEK.

140. The June 2002 Offer included an element for decommissioning. Slovenia states that the requested price of EUR 29.697 per MWh was, save for the decommissioning element, exactly the price that HEP would have been charged had the 2001 Agreement been in force.[143]

141. HEP did not accept this offer. HEP submits that it did not accept it because: (i) the establishment of a temporary buyer-seller relationship between itself and NEK would have jeopardised the 2001 Agreement; (ii) not having been involved in preparation of the 2002 Business Plan and establishment of electricity prices for 2002, it had no assurances that the prices were appropriate and calculated in accordance either with the Governing Agreements or the 2001 Agreement; and (iii) it was anxious that if the 2001 Agreement was not ratified by both sides and notices of such ratifications exchanged, it would run the risk of a new suspension of electricity deliveries at any time.[144]

142. Slovenia responds that: (i) there was no suggestion that Slovenia saw this arrangement as an alternative to ratification. The offer itself made it clear that it was intended to be a "stop gap" pending entry into force of the 2001 Agreement; (ii) the price was in substance identical to that which would have been payable under the 2001 Agreement. HEP could have proposed to accept the offer but for the part incorporating the decommissioning costs. Also, HEP had received NEK's proposed Business Plan for 2002 and therefore knew the basis on which the price was calculated; (iii) the electricity delivery to HEP had been suspended because HEP would not pay. This would not happen under the June 2002 Offer, since HEP would have been required to provide a bank guarantee for the event of non-payment.[145] Slovenia considers that the reason why HEP did not accept this offer was because it was able to purchase cheaper electricity elsewhere.[146]

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[142] Respondent's Counter-Memorial, paras 238-239

[143] Respondent's Counter-Memorial, para 240; Slovenia states in paragraph 241 of the Respondent's Counter-Memorial: "The June 2002 Offer included an element for decommissioning whereas under the 2001 Agreement HEP would not have had to pay this charge directly to NEK. However, as explained in section 5.2(c) above, NEK was nevertheless obliged by Slovenian law to include a charge for decommissioning in the price of electricity leaving the plant. In any event, under the 2001 Agreement Croatia agreed to meet its proportion of decommissioning costs and make regular payments into a separate fund as prescribed by Article 11 of the 2001 Agreement".

[144] Claimant's Memorial, paras 175-177

[145] Respondent's Counter-Memorial, paras 244-248

[146] Respondent's Counter-Memorial, paras 249-251

143. On 13 November 2002 NEK again offered to sell 50% of the electricity production of Krško NPP from 1 January 2003 to 31 December 2003.[147] The price requested was EUR 28.025 per MWh with a clearly delineated decommissioning element of EUR 2.0289 per MWh.[148] HEP rejected this offer for the same reasons.

IV. THE PARTIES' SUBMISSIONS

CLAIMANT'S SUBMISSIONS ON THE RESPONDENT'S LIABILITY UNDER THE 2001 AGREEMENT

144. Pursuant to Procedural Consent Order No.4, HEP filed its Submissions on Slovenia's Liability under the 2001 Agreement on 24 October 2008, contending that Slovenia had breached the 2001 Agreement and seeking a partial award to that effect.

145. HEP contended that the text of Exhibit 3 to the 2001 Agreement was unclear and ambiguous and that Slovenia's purely textualist approach to interpretation of the English translation of the "waiver provision" leads to a result that is "manifestly absurd....[and] unreasonable." Accordingly, HEP submitted that recourse was necessary to the applicable provisions of the VCLT, namely Articles 31 and 32, which require consideration of a wide range of interpretive sources, including the "preparatory work" and the "circumstances" in which the 2001 Agreement was concluded, in order to reach the correct interpretation of the parties' financial settlement. HEP emphasized that Exhibit 3 and the elements of the financial settlement it was intended to embody could not be understood without detailed background knowledge of the facts relevant to the parties' long-standing financial differences over the Krško NPP.

146. HEP further submitted that an examination of all such admissible material resulted in the conclusion that the essence of the parties' financial settlement was:

> that HEP's rights as a 50% owner of the Krško NPP, including its right to receive 50% of the electricity produced at the Krško NPP at a price jointly determined by HEP and its Slovenian counterpart, were to be restored on June 30, 2002; and (ii) that all parties were to waive all claims against one another through June 30, 2002.

147. HEP consequently submitted two alternative interpretations of the 2001 Agreement which it suggested would give effect to the parties' financial settlement based on a restoration of rights and their waiver of claims as of June 30, 2002, and the provision in Article 22(4) that the 2001 Agreement enters into force upon notice of ratification by both sides: (i) first, HEP contended that Slovenia choose, "with eyes wide open", to ratify the 2001 Agreement in February 2003, which included the financial settlement consisting of HEP's waiver of claims through June 30, 2002 and Slovenia's obligation to restore HEP's rights as a 50% owner of the Krško NPP by June 30, 2002. Since Slovenia failed to meet this deadline, HEP submitted that the Slovenia was liable to compensate HEP for its failure to meet the terms of the financial deal Slovenia agreed to in December 2001 and ratified in February 2003; and (ii) alternatively, HEP submitted that the only way to give effect to the intention of the parties (that HEP's losses from non-delivery of electricity were to be halted on

[147] Claimant's Memorial, para 179; Respondent's Counter-Memorial, para 252

[148] Respondent's Counter-Memorial, para 252

June 30, 2002, when Slovenia was obliged to restore HEP's rights as a 50% owner of the Krško NPP) was for the Tribunal to rule that the 2001 Agreement contained an implied term that required Slovenia to compensate HEP for all losses resulting from failure to restore HEP's rights as of June 30, 2002. HEP submitted that a failure to recognize such an implied term would be "wholly inconsistent with the principles of good faith and fair dealing."

RESPONDENT'S SUBMISSIONS ON THE TREATY INTERPRETATION ISSUE

148. Slovenia replied on 14 November 2008 with its Submissions on the Treaty Interpretation Issue. In these submissions Slovenia began by reiterating its view that even if the Tribunal were to find in HEP's favour on the Treaty Interpretation Issue, it could not issue a partial award on liability as that would require determination of the significance of the offers of supply, as to which the Tribunal had not heard all the relevant evidence.

149. Slovenia submitted that both theories proposed by HEP in their 24 October submission required HEP to establish that the 2001 Agreement was intended to create a retroactive legal obligation, with effect from 1 July 2002.

150. Slovenia contended, on the contrary, that the 2001 Agreement did not create any retroactive legal obligation. Instead, pursuant to Article 24 VCLT, the obligation to resume supplies to HEP and the financial settlement of past claims were to apply in tandem from the entry into force of the 2001 Agreement. Slovenia submitted that there was no intention to resume sales to HEP without the new legal framework in force, or to create an obligation to pay HEP compensation if supply was not restored by that date.

151. Slovenia further submitted that the general rule for treaty interpretation is found in Article 31(1) VCLT which stresses that the text of shall be interpreted in its context and in the light of its object and purpose. Whilst Slovenia acknowledged that recourse may be had to 'supplementary means of interpretation', pursuant to Article 32 VCLT, Slovenia contended that only a limited category of material would be admissible under this provision. Furthermore, Slovenia submitted that such supplementary aids to interpretation were to be considered secondary to the treaty text itself, which remained the "pre-eminent source for determining the parties' intentions."

152. In any event, Slovenia contended that there was no basis for referring to supplementary means of interpretation. The key terms governing the temporal scope of application of the 2001 Agreement, and in particular the obligation to supply electricity and the financial settlement and waiver, were clear, and did not render a result that was ambiguous or absurd.

CLAIMANT'S REPLY SUBMISSIONS ON THE RESPONDENT'S LIABILITY UNDER THE 2001 AGREEMENT

153. HEP contended in its Reply Submissions dated 19 November 2008 that Slovenia's entire case on the Treaty Interpretation Issue, stated in its 14 November submissions, rested on Article 28 VCLT and the presumption against retroactivity. HEP submitted that Slovenia had failed to deal with the evidence of the parties' intent in concluding their financial settlement. Further, HEP submitted that Slovenia had resorted to an

argument that the parties merely expected that HEP's rights would be restored by 30 June 2002, suggesting that this date was only of political significance. By contrast, HEP submitted that the 30 June 2002 date was an integral element of the 2001 Agreement. Furthermore, HEP contended that whether the agreement is analyzed in terms of: (i) the exceptions to the presumption against retroactivity found in Article 28 VCLT; (ii) Slovenia's ratification of an agreement that expressly called for restoration of HEP's rights in the Krško NPP by June 30, 2002; or (iii) an implied obligation to compensate HEP for the non-deliveries of electricity from July 1, 2002, the issue of HEP's rights to compensation turn on the intention of the parties. Consequently, evidence supported the conclusion that the parties intended to resolve their financial differences by the restoration of HEP's rights on June 30, 2002 and to exchange mutual waivers through that date.

CLAIMANT'S SUBMISSIONS ON IMPLIED TREATY TERMS

154. In response to the Tribunal's invitation of 25 November 2008, the Claimant filed its comments on the Iran–United States Claims Tribunal case, mentioned by Judge Brower on 25 November 2008, and to respond to a question raised by Mr Paulsson in the course of the November hearing in Paris. In this case an "implied" obligation had been recognized in an international arbitral award.

155. HEP replied in the affirmative to the Tribunal's question of whether treaty terms could be implied. In support of this contention HEP made the following submissions:

- There is authority supporting an award of compensatory damages based on a State's breach of an implied term in a treaty.
- In *Islamic Republic of Iran v. United States of America,* Partial Award No. 382-B1-FT (31 August 1988), 19 Iran-U.S Cl. Trib. Rep. 273 (1988) and *Islamic Republic of Iran v. United States of America,* Partial Award No. 529-A15-FT (6 May 1992), 28 Iran-U.S Cl. Trib. 112 (1992) the Iran-United States Claims Tribunal found obligations to be "implied" in the Algiers Accords – in one case to compensate for property acquired, and in the other to compensate "any losses" that might be proven, in both cases in later proceedings.
- In both these cases, the Tribunal held that the United States had an implied obligation to compensate Iran because to find otherwise would have been inconsistent with the object, purpose and intention of the agreement between the parties, an essential objective of which had been to restore Iran's financial position on a specified date.
- The circumstances presented to the Iran-United States Claims Tribunal in both these cases are the same as those confronting the Tribunal in the present case. Therefore terms must be implied in the present case, in order not to frustrate the essential purpose of the 2001 Agreement.
- Aside from those cases in which compensatory damages have been awarded, international tribunals have routinely issued awards to remedy breaches of implied treaty obligations. HEP supported this contention with reference to *Islamic Republic of Iran v. United States of America,* Partial Award No. 597-A11-FT (7 April 2000), ___Iran- U.S. Cl. Trib. __ ; *Velasquez-Rodriguez Case,* Merits

Judgment, Inter-Am. Ct. H.R (ser.C) No. 4 (July 29, 1988); *Marckx v Belgium,* App. No 6833/74, 1980 WL 115477 (Eur. Ct. H.R June 13, 1979); *Jabari v Turkey,* App. No. 40035/98, 2000 WL 33201699; *Tanzania Electric Supply Company Ltd. V. Independent Power Tanzania Ltd.,* ICSID Case No. ARB/98/8, Award (July 12, 2001), 8 ICSID Rep. 226 (2005); *United States v Rauscher,* 119 U.S. 407 (1886), *Regina (Middleton) v. West Somerset Coroner,* [2004] 2 A.C 182; *R v. Marhsall,* 1999 Can. Sup. Ct. LEXIS 77; *Regina v. Sundown* [1999]]1 S.C.R 393; *R v. Sioui* [1990] 1 S.C.R. 1025; *South West Africa (Ethiopia v. South Africa; Liberia v. South Africa),* Second Phase, 1966 I.C.J 6 (July 18).

- In accordance with the principles and reasoning applied by the Iran-United States Claims Tribunal, the ECHR, the ICJ and the highest courts of various domestic jurisdictions, the Tribunal should find that Slovenia implicitly agreed to pay HEP damages in the event that Slovenia breached the agreement to resume electricity deliveries to HEP by 30 June 2002.

RESPONDENT'S SUBMISSIONS ON *CASE A15*

156. On 12 December 2008, Slovenia filed the following submissions regarding the Iran-United States Claims Tribunal case, *Case A15.*[149]

- *Case A15* was one of the few examples in public international law where a State has been held to owe obligations by virtue of an implied term. The case does not, however, advance the position that Slovenia may have been under an implied obligation to compensate HEP for electricity not delivered after 30 June 2002.

- There was no discussion in *Case A15* of the relevant international law concerning the "highly controversial" question of whether a tribunal may imply a term into a treaty. Instead, weight must be given to the many decisions of courts and tribunals which have held that it would be inappropriate to imply terms. In any event, decisions such as *Case A15* are not binding and have only persuasive value.

- In *Case A15* the term implied was that "General Principle A and paragraph 9" of the agreement between the parties (the "General Declaration") implied an obligation to compensate Iran for any "losses" it experienced as a result of the United States lawfully refusing to permit exportation to Iran from the United States of Iranian-owned military properties. However, Slovenia contended that in the present case underlying obligations such as General Principle A do not exist. Instead, HEP had asked the Tribunal to imply both an underlying obligation (i.e. to restore HEP's rights from 30 June 2002 in the absence of the Treaty being in force), and an obligation to pay compensation to HEP flowing from its breach. Slovenia did not accept that there ever was such an underlying obligation. Consequently, there cannot be an implied obligation to compensate.

- In *Case A15* there was evidence from both Iran and the United States as to their common intention concerning the interpretation of General Principle A and paragraph 9 of the General Declaration. In contrast, Slovenia contends that an implied term was never intended here.

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[149] *Islamic Republic of Iran v. United States of America,* Partial Award No.529-A15-FT, 6 May 1992, 28 Iran-U.S C.T.R 112

- *Case A15* was itself highly controversial as three members of the Iran-United States Claims Tribunal dissented on the relevant point. Further, *Case A15* formed part of a "unique and highly complex factual matrix", which was very different to the facts of the present case.

V. RELEVANT PRINCIPLES OF TREATY INTERPRETATION

157. Before examining the substantive issues in its decision, the Tribunal sets out the relevant principles of treaty interpretation which have guided it in its approach to interpreting the 2001 Agreement.

158. The Vienna Convention on the Law of Treaties 1969 ("VCLT") is recognised in international law as the primary statement of the principles governing the construction and interpretation of treaties. Article 31 VCLT provides that:

> **Article 31: General rule of interpretation**
>
> 1. A treaty shall be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose.
>
> 2. The context for the purpose of the interpretation of a treaty shall comprise, in addition the text, including its preamble and annexes:
>
> (a) any agreement relating to the treaty which was made between all the parties in connection with the conclusion of the treaty;
>
> (b) any instrument which was made by one or more parties in connection with the conclusion of the treaty and accepted by the other parties as an instrument related to the treaty.
>
> 3. There shall be taken into account, together with the context:
>
> (a) any subsequent agreement between the parties regarding the interpretation of the treaty or the application of its provisions;
>
> (b) any subsequent practice in the application of the treaty which establishes the agreement of the parties regarding its interpretation;
>
> (c) any relevant rules of international law applicable in the relations between the parties.
>
> 4. A special meaning shall be given to a term if it is established that the parties so intended.

159. Much has been written about Articles 31 and 32 of the VCLT.[150] As to Article 31 of the VCLT, a helpful recent discussion of the principles of treaty interpretation set out in that Article may be found in the judgment of Justice Simon in *Czech Republic v European Media Ventures SA* [2008] 1 All E.R. (Comm) 531:

At paragraphs 16-17:

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[150] *See, e.g.*, Shaw International Law (5th Ed 2003) 838-844 and authorities cited therein

It is clear that the proper approach to the interpretation of Treaty wording is to identify what the words mean in their context (the textual method), rather than attempting to identify what may have been the underlying purpose in the use of the words (the teleological method). The disadvantages of this latter approach have been described ...as follows:

> One method ....is to ask the question: "What did the parties intend by the clause?" This approach has, however, been felt to be unsatisfactory, if not actually unsound and illogical, for a number of reasons....It ignores the fact that the treaty was, after all, drafted precisely in order to give expression to the intentions of the parties, and must be presumed to do so. Accordingly this intention is, *prima facie*, to be found in the text itself, and therefore the primary question is not what the parties intended by the text, but what the text itself means: whatever it clearly means on an ordinary and natural construction of its terms, such will be deemed to be what the parties intended....the aim of giving effect to the intentions of the parties means, and can only mean, their *joint* or *common* intentions...This means that, faced with a disputed interpretation, and different professions of intention, the tribunal cannot in fact give effect to any intention which both or all the parties will recognise as representing their common mind... [citation omitted.]

The search for a common intention is likely to be both elusive and unnecessary. Elusive, because the contracting parties may never have had a common intention: only an agreement as to a form of words. Unnecessary, because the rules for the interpretation of international treaties focus on the words and meaning and not the intention of one or other contracting party, unless that intention can be derived from the object and purpose of the Treaty [article 31 of the Vienna Convention], its context [article 31.1 and 31.2] or a subsequent agreement as to interpretation [article 31.3(a)] or practice which establishes an agreement as to its interpretation [article 31.3(b)].

At paragraph 19:

> The proper approach is to interpret the agreed form of words which, objectively and in their proper context, bear an ascertainable meaning. This approach, no doubt reflecting the experience of centuries of diplomacy, leaves open the possibility that the parties might have dissimilar intentions and might wish to put different interpretations on what they had agreed. When considering the object and purpose of a treaty a court should be cautious about taking into account material which extends beyond what the contracting parties have agreed in the preamble or other common expressions of intent, see article 31.2(a) and (b).

At paragraphs 36-37:

> ...the "ordinary meaning" is the meaning attributed to those terms at the time the treaty is concluded...the terms of the treaty must be interpreted according to the meaning which they possessed, or which would have been attributed to them, and in light of current linguistic usage, at the time when the treaty was originally concluded....as a normal principle of interpretation a court or tribunal should endeavour to give a meaning to each of the words being interpreted.

160. Following the application of Article 31, further recourse may be had to Article 32 VCLT, in the circumstances, or for the purpose, described therein. Article 32 provides:

> **Article 32: Supplementary means of interpretation**
>
> Recourse may be had to supplementary means of interpretation, including the preparatory work of the treaty and the circumstances of its conclusion, in order to confirm the meaning resulting from the application of article 31, or to determine the meaning when the interpretation according to article 31:
>
> (a) leaves the meaning ambiguous or obscure;

(b) leads to a result which is manifestly absurd or unreasonable.

161. Article 24 governs the manner in which a treaty will enter into force:

Article 24: Entry into force

1. A treaty enters into force in such manner and upon such date as it may provide or as the negotiating States may agree.

2. Failing any such provision or agreement, a treaty enters into force as soon as consent to be bound by the treaty has been established for all the negotiating States.

3. When the consent of a State to be bound by a treaty is established on a date after the treaty has come into force, the treaty enters into force for that State on that date, unless the treaty otherwise provides.

4. The provisions of a treaty regulating the authentication of its text, the establishment of the consent of States to be bound by the treaty, the manner or date of its entry into force, reservations, the functions of the depositary and other matters arising necessarily before the entry into force of the treaty apply from the time of the adoption of its text.

162. Article 28 is also relevant, establishing the general rule against retroactivity in the following terms:

Article 28: Non-retroactivity of treaties

Unless a different intention appears from the treaty or is otherwise established, its provisions do not bind a party in relation to any act or fact which took place or any situation which ceased to exist before the date of the entry into force of the treaty with respect to that party.

VI. DISCUSSION

163. The starting point in order to ascertain the true interpretation of the 2001 Agreement is Article 31 of the VCLT. As noted above, that article requires a treaty to be interpreted in accordance with the ordinary meaning to be given to the terms of treaty in their context and in the light of its object and purpose. Moreover, Article 31(3) stipulates that, together with the "context", it is necessary to take into account any subsequent agreement between the parties regarding the interpretation or application of the treaty, any subsequent practice in the application of the treaty and any relevant and applicable rules of international law.

164. The International Law Commission has emphasised in relation to Article 31 that there is no legal hierarchy between the various aids to interpretation outlined in that Article. In this regard, the International Law Commission has observed that "[t]he application of the means of interpretation in this article would be a single combined operation" and that "[a]ll the various elements [terms, context, object and purpose] would be thrown into the crucible, and their interaction would give the legally relevant interpretation."[151]

165. Article 32 further provides that recourse may be had to extrinsic evidence in order to "confirm" the meaning resulting from the application of Article 31 or to determine the

[151] *Yearbook of International Law Commission,* 1966, vol. II at pp 219-220

meaning when the application of Article 31 leaves the meaning "ambiguous or obscure" or "manifestly absurd or unreasonable."

THE TRIBUNAL'S JURISDICTION

166. A threshold issue is whether under the 2001 Agreement, to which only Croatia and Slovenia are parties, this Tribunal has jurisdiction over the dispute presented to it. More precisely, can HEP bring this case against the Republic of Slovenia and before us? Issues of jurisdiction were not seriously contested between the parties to this arbitration; nevertheless, some questions were asked and in any event the Tribunal is obliged to be satisfied of its jurisdiction.

167. The issue is readily settled. Article 19 of the 2001 Agreement, entitled "(Dispute Resolution)," provides in its Paragraph 2(e) that "[if] a dispute ['between one Contracting Party and the members of the Company from the other Contracting Party'] cannot be settled amicably ..., the aggrieved Shareholder may ... refer the dispute for resolution to [ICSID]." "Company" is defined in Article 2(1) as "NEK d.o.o.," and both HEP and ELES GEN are defined in the same Article 2(1) as "Shareholders."

168. Clearly the dispute before the Tribunal is one to enforce Article 17 and Exhibit 3 of the 2001 Agreement. The two State Parties to that Agreement have entered into it as the ultimate shareholders of the immediate "Shareholders" of NEK d.o.o. The Agreement establishes in detail the points generally included in a shareholders agreement. In doing so it gives their respective wholly-owned immediate "Shareholders" of NEK d.o.o. the right to arbitrate directly against the "other State Party" for any failure on the latter's part to cause its wholly-owned "Shareholder" to comply with the Agreement. Moreover, in Article 12(1)2. of the Agreement (entitled "Protection of Investments") "[t]he Contracting Parties agree ... that they shall ensure fair and impartial treatment of the Shareholders belonging to the other Contracting Party on their territories, i.e. that they shall treat such Shareholder the same way as its own Shareholder, with full protection and security of investments for the duration of the joint investment."

169. The Tribunal is in no doubt as to its jurisdiction to hear and decide the dispute here presented to it.

THE TREATY'S TERMS

170. The crux of the issue before the Tribunal is the correct interpretation to be adopted of Article 17 and Exhibit 3 of the 2001 Agreement. It will be recalled that Article 17 provides:

> Past Financial Issues
>
> (1) Mutual financial relations existing up to the signing of this Agreement between NEK d.o.o., ELES d.o.o., and HEP d.d. shall be regulated in accordance with the principles set forth in Exhibit 3 of this Agreement.
>
> (2) The Contracting Parties agree that, as of the date of entry into force hereof, all obligations of NEK d.o.o. to the Fund for financing the dismantling of NE Krško and disposal of radioactive waste from NE Krško, which obligations arose from the

> application of the Act on Fund for Financing of Dismantling of NE Krško and Disposal of Radioactive Waste from NE Krško... shall cease to exist.

171. The reference in Article 17(1) to "[m]utual financial relations existing up until the signing of this Agreement [which] shall be regulated in accordance with the principles set forth in Exhibit 3 of this Agreement" naturally must be read together with the Article's heading, "Past Financial Issues," and also with the reference in Article 17(2) to "which obligations arose." (It is to be noted that the 2001 Agreement, unlike many agreements, has no express provision depriving headings of interpretative value, and that the VCLT also has no such provision.) Plainly the text provides for the "regulat[ion] in accordance with the principles set forth in Exhibit 3 of this Agreement" of "financial issues" that had arisen between the parties prior to the signing on 19 December 2001 of the 2001 Agreement. That is to say, it speaks of a settlement, on the basis set forth in Exhibit 3, of outstanding disputes.

172. Article 17(1) makes Exhibit 3 an integral part of the entire 2001 Agreement. This is confirmed by the fact that Articles 2(3), relating to Exhibit 1 to the 2001 Agreement ("Memorandum of Association"), and 18(2), relating to Exhibit 4 ("Bilateral Committee Rules of Procedure"), state, respectively, "The executed Memorandum of Association is not an integral part of this Agreement" and "The Rules of Procedure ... are not considered an integral part of this Agreement." The lack of an express statement to the contrary, therefore, confirms that Exhibit 3 is to be treated as an integral part of the 2001 Agreement.

173. Exhibit 3 of the 2001 Agreement, which regulates the past "financial relations" between the parties, has already been set out, but to assist the analysis it is set out again here:

> PRINCIPLES OF THE STRUCTURING OF THE FINANCIAL RELATIONS
>
> (1) ELES GEN d.o.o. shall assume all obligations of NEK d.o.o towards the bank which have occurred as a result of the transfer to NEK d.o.o of the repayment of investment loans made by the Slovene founders, according to the balance on December 31, 2001. Obligations resulting from loans issued to carry out NEK's modernization project will be NEK d.o.o's only remaining long-term financial obligations. Until June 30, 2002, the cost of these loans will be borne through the cost of electricity by the Shareholder from the Republic of Slovenia and from that day forward by both Shareholders.
>
> (2) By virtue of the entry into force of this Agreement:
>
> -HEP d.d. waives all claims against NEK d.o.o for damages, i.e. for compensation for undelivered electricity, i.e. for compensation for use of the capital, and in this regard will fully waive all claims in court arising therefrom;
>
> -NEK d.o.o waives all claims against HEP d.d. in connection with delivered power and electricity, and in this regard will fully waive all claims in court arising therefrom;
>
> -NEK d.o.o waives its claims against ELES d.o.o in the same amount as in the previous bullet of this Paragraph;
>
> -NEK d.o.o. waives all claims against HEP d.d. in connection with charged fees for financing of the dismantling of the Nuclear Power Plant Krško and disposal of radioactive waste from Nuclear Power Plant Krško, and in this regard will fully waive any claims in court arising therefrom;

-NEK d.o.o. waives all claims in connection with pooled resources of depreciation of both founders and claims in connection with the coverage of losses from previous years.

(3) Based on the provisions listed above, NEK d.o.o will rearrange its balance sheet on December 31, 2001 so that:

-it shows neither any claims toward HEP d.d. and ELES d.o.o nor any obligations toward the fund for financing of the dismantling of the Nuclear Power Plant Krško and the disposal of radioactive waste from the Nuclear Power Plant Krško;

-it does not show any obligations toward the bank which occurred as a result of the transfer of repayment of Slovene founders' investment loans to NEK d.o.o. described in Paragraph 1 of this Exhibit;

-based on the conversion of HEP's long term investments and the exemption of the loan, NEK d.o.o's capital will, after the payment of the possible uncovered losses, be distributed to the Shareholders in two equal parts, so that the initial capital of NEK d.o.o. reaches the amount listed in Article 2 of this Agreement, and so that any possible remainder is distributed into the reserves;

-any other necessary accounting corrections or changes arising from this Exhibit are executed.

(4) Any possible profit to NEK d.o.o. arising from accounting corrections or changes described in Paragraph 3 of this Exhibit will be tax-exempt.

(5) ELES GEN d.o.o assumes the financial results of all power and electricity produced during the period from July 31, 1998 until the date HEP d.d. begins to take over the electricity again, but no later than June 30, 2002. All the while, NEK d.o.o.'s financial position must not worsen compared to its financial position on July 30, 1998.

(6) The Contracting Parties will ensure that the Shareholders determine, by no later than the end of 2002, whether the company needs additional long-term sources of financing its operating costs, which sources of financing will be secured by a capital increase in NEK d.o.o. or any other appropriate manner.

174. Exhibit 3 is entitled "Principles of the Structuring of Financial Relations". Its paragraph (1) provides that ELES GEN d.o.o. shall be responsible for the repayment of investment loans by the Slovene founders of NEK "according to the balance on December 31, 2001," and that NEK's responsibility for "remaining long-term financial obligations" arising out of "NEK's modernization project" "will be borne through the cost of electricity by the Shareholder from the Republic of Slovenia [until June 30, 2002] and from that day forward by both Shareholders." This of course is in line with the parity principle that has governed the two sides since the 1970 Agreement and which permeates the 2001 Agreement (see Paragraphs 196-197, below). Accordingly, HEP's post-30 June 2002 obligation to share NEK's previously incurred modernization costs is part of the financial settlement achieved by Article 17 and Exhibit 3 of the 2001 Agreement. That settlement is a two-way street. Paragraph (5) provides that ELES GEN "assumes the financial results of all power and electricity produced during the period from July 31, 1998 until the date HEP d.d. begins to take over the electricity again, but no later than June 30, 2002." Hence, starting 1 July 2002, HEP would share the costs outlined in paragraph (1) in accordance with the new financial terms and, as of 1 July 2002 HEP would also be entitled to the financial results of its share of the electricity produced by Krško NPP. While of course NEK could not be compelled actually to deliver electricity to HEP until such time as the 2001 Agreement would enter into force, the terms of the

financial settlement concluded, and which perforce took effect with the entry into force of the 2001 Agreement, were based on the financial facts that would flow had HEP been supplied electricity starting 1 July 2002.[152]

175. Just as Exhibit 3 determines the date as of which the new financial terms would take effect, i.e., on the "critical date" of 30 June 2002, so, too, does it determine the extent of the waivers contained in Paragraph (2) of Exhibit 3. Paragraph (2) expressly refers to "delivered" and "undelivered" electricity without also giving a date against which electricity is to be classified as "delivered" or "undelivered". The same applies to the subsequent waivers in which NEK waives "all claims against HEP" relating to the dismantling of the Krško NPP, disposal of waste, "depreciation" and "coverage of losses from previous years."[153]

176. It is important to note that the above view is reached as a result of construing the words of the 2001 Agreement as prescribed by Articles 31 and 32 of the VCLT. Nothing more and nothing less. While the parties have debated vigorously the issue of whether an obligation can be "implied" in an international agreement, that debate is rendered pointless by the terms of VCLT Articles 31 and 32, which do not categorize treaty provisions as being either "express" or "implied". Hence the VCLT-prescribed interpretive process is just that. No greater or lesser force resides in a term by virtue of the relative magnitude of the clarity with which it has been (or has not been) written. The Tribunal's construction of Article 17 and Exhibit 3 becomes clearer still when, as the VCLT requires, one considers their wording "in light of the [the 2001 Agreement's] object and purpose" and "in their context."

OBJECT AND PURPOSE

177. Turning to the object and purpose of the 2001 Agreement, the Tribunal concludes that the 2001 Agreement was in general terms a settlement agreement intended to resolve the longstanding and significant differences between the two countries and to thereby enable the resumed joint operation and exploitation of NPP Krško in accordance with the parity principle. In other words, the purpose of the 2001 Agreement was to draw a line in time, on 30 June 2002, as of which all past financial disputes were to be settled and from which new financial terms were to take effect, with a "zero/zero" financial balance to be achieved, as of 1 July 2002.

178. It is agreed between the parties that, at the time of the signing, both parties envisaged that the 2001 Agreement would have entered into force prior to the agreed "critical

[152] While eventual decommissioning costs paid by or charged to HEP prior to 1 July 2002 were waived per the penultimate bullet point in Paragraph (2) of Exhibit 3, the parity principle is upheld in this respect, too, by Articles 10 ("Dismantling, Radioactive Waste and Spent Nuclear Fuel") and 11 ("Financing of Dismantling and Disposal") of the 2001 Agreement as regards the totality of such costs. Those Articles both read in the future, i.e., expressly leaving the various elements of the process to commence within stated numbers of days "from the entry into force of this Agreement," or "from the date of entry into force hereof." Thus the unexpectedly delayed entry into force of that Agreement had no effect on the parity principle in that regard or on the financial settlement keyed to the "critical date" of 1 July 2002. Hence in benefiting as claimed, and found by the Tribunal, as regards the costs of electricity beginning 1 July 2002 HEP in no way escapes its obligation to contribute its 50 percent share of ultimate decommissioning costs.

[153] The fact that Paragraph (2) of Exhibit 3 is prefaced by the phrase "By virtue of the entry into force of the Agreement" is of no interpretive value. It simply confirms the obvious, namely that the Agreement could enter into force only upon the exchange of the State Parties' respective notes of ratification.

date" of 30 June 2002 and that the 2001 Agreement's terms would therefore already have become enforceable. That the ratification became delayed and the timetable intended by the parties in 2001 for the practical implementation of the 2001 Agreement never eventuated did not affect the fundamental object and purpose of the 2001 Agreement as embodied in its text. Instead, the object and purpose remained to provide for the resumed 50-50 operation and exploitation of Krško NPP by entering into a liquidated financial settlement of all claims existing as of the 2001 Agreement's signature, which settlement was keyed to the presumed time of entry into force of the 2001 Agreement, and which claims would be measured with reference to the date on which a "zero/zero" financial balance was deemed to occur.

179. The object and purpose as outlined above is reflected in Paragraph (ii) of the preamble to the 2001 Agreement, which provides:

> (ii) having a desire, as sovereign and internationally recognised states, to continue to jointly regulate their relations regarding the status, use and dismantling of Nuclear Power Plant Krško [...]

180. On a practical level, the terms of the 2001 Agreement, with the exception of the provisions of Exhibit 3, amount to a reincarnation of the terms of the 1970 Agreement and the parity principle contained therein. On its entry into force the 2001 Agreement replaced the 1970 Agreement (Article 22, Paragraph (1)). In addition to replacing the 1970 Agreement, the 2001 Agreement:

- recognizes HEP and ELES-GEN as the legal successors in interest to the Slovenian and Croatian companies that invested in the construction of Krško NPP (Article 1(a));
- provides that HEP and ELES-GEN will have equal rights and obligations, unless otherwise stated into the Agreement (Article 1(b));
- establishes HEP and ELES-GEN as 50:50 shareholders in the limited liability company NEK, a new legal entity to be governed by a Memorandum of Association (Exhibit 1 to the 2001 Agreement. The Memorandum of Association states in Article 2 that the transformation of NEK will take place in accordance with the 2001 Agreement and Slovenian company law. It also provides in its Article 30 the possibility for NEK to terminate electricity deliveries to the shareholder who fails to comply with its financial obligations.) (Article 2);
- states that the governance of NEK will be exercised in accordance with the parity principle. ELES-GEN nominates the Chairman of the Management Board and HEP the Vice-Chairman. HEP nominates the Chairman of the Supervisory Board and ELES-GEN the Vice-Chairman. The Chairman of the Management Board has a casting vote, controlled however by the Supervisory Board (Article 3);
- orders that electricity produced at the Krško NPP shall be delivered to the shareholders in equal proportions (Article 5);

- states that the price for electricity deliveries comprises operating costs, including, *inter alia*, the depreciation costs, in the amounts necessary for long-term investment; and

- stipulates that decommissioning and radioactive waste disposal are joint liabilities of Croatia and Slovenia and will be financed in equal proportions. The funds for decommissioning shall be collected in a special fund created by each State (Articles 10 and 11).

THE TREATY'S CONTEXT

181. Considering "context" within the meaning of Article 31(2) of the VCLT, the only "agreement relating to the treaty which was made between *all the parties* [i.e., Slovenia and Croatia] in connection with the conclusion of the treaty" (emphasis added), could be the "Joint Statement" signed together with the Treaty on 19 December 2001 by the Croatian Minister of Economy, Mr Fizulic, and the Slovenian Minister of Environment and Planning, Mr Kopac.

182. The parties disagree slightly over the precise translation of this "Joint Statement", but it is not disputed that it provides:

> (1) Regarding the time component built into the [2001 Agreement] and the necessary extensive preparations for its implementation, the two Parties shall do their best to ensure [HEP version] / shall endeavour [Slovenia version] that the ratifications of the [2001 Agreement] in the Croatian Parliament and the Parliament of the Republic of Slovenia are implemented as soon as possible during the first quarter of 2002.
>
> (2) For the entry into force of the Memorandum of Association [Exhibit 1]. . . and for the review of the balance sheets according to Clause 3 of [Exhibit 3], the first appropriate dates shall be chosen (first date of the month and the last date of the previous month) after the entry into force of [the 2001 Agreement], but no later than the second quarter of 2002.
>
> (3) According to the Joint Minutes on the completion of negotiations of July 5, 2001, the joint committee for the preparation of the basis required for the constitutional meeting of the company and other actions important for the efficient start-up operation of the company shall commence its work on January 7, 2002, and as part of its work include the review of the annual plan for 2002, and other documents of importance for the operation of [the Plant].

This Joint Statement is entirely consistent with, and indeed further confirms, the Tribunal's textual analysis.

ARTICLE 32 OF THE VIENNA CONVENTION

183. The result arrived at above by applying Article 31 to the 2001 Agreement is confirmed on further investigation pursuant to Article 32, which permits reference to the *travaux* of a treaty in order to confirm the meaning resulting from the application of Article 31. Alternatively, should application of Article 31 be seen as leaving the meaning "ambiguous or obscure," or, indeed, "manifestly absurd or unreasonable," resort to Article 32 produces the same result as the Tribunal's foregoing textual analysis. Viewed in light of the drafts and documents prepared by the two sides in conjunction with the various stages of the negotiations, as amplified by the testimony

of key actors present during those negotiations, the interpretation outlined above emerges as the only interpretation which adequately reflects the parties' mutual intentions and is therefore confirmed.[154]

184. Slovenia itself has argued that the 2001 Agreement constituted an agreement to "deem their financial relations to be balanced as of six months after the expected date of entry in force of the 2001 Agreement," which at the time of the Rijeka meeting was expected to be 1 January 2002.[155] Clearly it was the intent of both parties to draw a line in time as of which all past financial disputes were settled and from which new financial terms were to take effect. That line in time became 30 June 2002.

185. In May 2001 Dr Goran Granic, Deputy Prime Minister of Croatia from 2000 to 2003, originated the essential features of what became Exhibit 3, namely, that the solution to the longstanding and significant differences between the two countries was to "wipe the slate clean" as of an agreed future "critical date" as of which all claims would be waived, electricity deliveries would be resumed, and the two shareholders would co-own and co-manage NEK.[156]

186. At the meeting of the Prime Ministers of Croatia and Slovenia in Rijeka, Croatia on 9 June 2001, the Croatian Prime Minister, Mr Ivica Racan, and his delegation, including Dr Granic, put this proposal to the Slovenian representatives and they found this acceptable. The Croatian side then proposed 1 January 2002 as the "critical date," and the Slovenians countered with 30 June 2002, which the Croatians quickly accepted, and the two sides agreed each to draft their understanding of this agreement for final negotiations at a future session.[157] The final text of what became Exhibit 3 was finalized at a 28-30 June 2001 meeting at Brijuni, Croatia, and the entire text of what became the 2001 Agreement was completed at a 5 July 2001 meeting in Otocec na Krki, Slovenia.

187. Dr Granic states that without the agreement on the Slovenian side in these negotiations to take responsibility for electricity deliveries to Croatia as of 30 June 2002, Croatia and HEP would not have agreed to waive their claims against NEK and ELES as from 31 July 1998 until that date, after which point HEP would stop incurring further damages for non-delivery.[158] Memoranda authored by Mr Korze, who was the head of the Slovenian negotiating team for the 2001 Agreement, in June and July 2001 each indicate that "all of the electricity will be delivered to the Slovenian Shareholder until 1 July 2002, and from this date on each of the Shareholders will receive one half of electricity" and, likewise, that the Slovenian side would:[159]

[154] It may be recalled from *Czech Republic v. European Media Ventures SA* (paragraph 171 above) that only in the event of "different professions of intention" by the treaty parties are their professions of intent to be ignored.

[155] Respondent's Counter Memorial, para 206; *see also* Ogorevc Witness Statement ("WS") at paras 23-24.

[156] Granic WS, paras 14-15

[157] Granic WS, paras 19-20; Tr., Day 6 at 109-112

[158] Tr. Day 6 at 112:20-25

[159] Tr. Day 3 at 102-105; Exhibits C-307, C-310, and C-311 at paras 8-9.

> cover all costs and [. . .] assume all financial results in connection with assumption of electricity from 1 August 1998 until the date of resumption of electricity supplies to HEP, but no later than 30 June 2002.

188. Both sides' drafts brought to the Brijuni negotiating round stated that HEP's right to receive electricity from the Krško NPP would be restored "on" (Croatian draft [Ex. C-181 cl. 8]) or "by" (Slovenian draft [Ex. C-182 cl. 4]) 30 June 2002.[160] Also, in its later filing in the Slovenian Constitutional Court in connection with a challenge to the constitutionality in Slovenia of the 2001 Agreement, the Slovenian Government affirmed that HEP was to "start receiving, no later than 1 July 2002, one half of the electricity generated by NEK."[161]

189. The delay of the entry into force of the 2001 Agreement until 2003 did not affect the parties' mutual intention in signing the 2001 Agreement on 19 December 2001 that Slovenia's *financial responsibility* for electricity deliveries to Croatia be revived, and the waivers end, as of 30 June 2002. The Tribunal agrees with the Claimant's submission that:[162]

> [t]he obvious and natural result of the unforeseen delay [in ratification and entry into force] was that, if the Rijeka agreement was still to be put into effect, both Governments should be held to the terms of that initial agreement, regardless of the timing of ratification.

190. Slovenia's suggestion at various other points that the 30 June 2002 date was intended to represent only a "relative," "fictional," or "notional" equilibrium is not supported by the evidence. Slovenia has argued that the intent was that the parties would "deem their financial relations to be balanced as of six months after the expected date of entry into force of the 2001 Agreement," which at the time of the Rijeka meeting was expected to be 1 January 2002.[163] This arrangement, according to Mr. Ogorevc, who was Slovenia's negotiator on what became the text of Exhibit 3, was agreed so as "to give both parties sufficient time to put into place the necessary conditions for the implementation of the 2001 Agreement."[164] The 2001 Agreement was not actually signed until 19 December 2001, however, and there is no indication that performance of the 2001 Agreement would hinge either on it being in force as soon as 1 January 2002 or on there being a six-month implementation window thereafter. Of course, the 2001 Agreement did specify dates at which various acts were to be taken, and were taken, before the 2001 Agreement's entry into force.[165] Slovenia also has conceded that, had the 2001 Agreement been ratified after 1 January 2002 but before 30 June 2002, the obligation to restore electricity deliveries would have arisen regardless as of 1 July 2002.[166] It strains credibility for Slovenia on the one hand to characterize Exhibit 3 as embodying a "financial settlement" but for it also to argue on the other hand that the basic "price" of this settlement – that ELES would enjoy the "financial results" of electricity generation minus the "cost" of the

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[160] Claimant's Reply, para 237

[161] Exhibit C-315; Tr. Day 3 at 106-107

[162] Claimant's Reply, para 270

[163] Respondent's Counter-Memorial, para 206; *see also* Ogorevc WS, paras 23-24

[164] Ogorevc WS, para 23

[165] *See*, e.g., Article 2(3) ("The company founders shall enter into the Memorandum of Association immediately upon the execution of this Agreement"); Exhibit 3 at (3)("NEK d.d. will rearrange its balance sheet on December 31, 2001")

[166] Tr. Day 6 at 66:6-19

modernization loans "until June 30, 2002" – was somehow "fictional," "notional," or "relative."

GOOD FAITH

191. It is to be remembered that VCLT Article 31 mandates that treaties be interpreted "in good faith." That is the core principle about which all else revolves. The Tribunal is persuaded that a good faith interpretation of the 2001 Agreement compels the conclusion at which it has arrived. That result does no violence, either to the Agreement's language or in its result. As both parties agree was their desire, a line is drawn as of 30 June 2002 under their earlier differences, and upon entry into force HEP receives what was agreed, i.e.: full implementation of the parity principle as regards NKK Krško; mutual waivers of all claims existing as of 30 June 2002; and an equal share in the financial benefits, calculated from 1 July 2002, accruing to a 50-percent offtaker of NEK's produced power. Those benefits must take into account, however, that as of 1 July 2002 HEP must bear 50 percent of the modernization costs incurred in the past. That obligation is built into the valuation of the electricity that HEP notionally would have received in the event of the 2001 Agreement entering into force before 1 July 2002. Furthermore, HEP must, by other means prescribed in the 2001 Agreement, provide 50 percent of all of the decommissioning costs that ultimately will be incurred. In no way does it get a "free ride" for the nine and a half months before it once more actually received electricity on 19 April 2003 following the 2001 Agreement's entry into force.

192. Conversely, the Respondent (or ELES GEN or NEK) bears the same liabilities it would have had if the Agreement had entered into force prior to 1 July 2002. It will be recalled (see Paragraph 131, above) that, as spelled out by the Respondent in its Rejoinder:[167]

> [t]here is a distinction to be drawn between physical flows of electricity and how that electricity is purchased. A person may physically acquire electricity from persons other than from persons with whom it contracts to purchase it. Contracts may change, but the physical flows do not. The Tribunal should not be under any misapprehension that HEP or Croatia were deprived of actual energy flows from the Krško NPP. In fact, apart from a very brief period 10 years ago – just a few days – there was no physical cut-off at all. Even then, only two of the several transmission lines from Slovenia to Croatia were affected. Beyond this, throughout the whole of the relevant period Croatia continued to receive electricity from the Krško NPP in exactly the same way as it had done before July 1998 and indeed does so today. Zagreb continued to be powered by the electricity of the Krško NPP. Rather than any physical termination of electricity supply, what occurred is merely that on the contractual plane (i.e. as a matter of accounting or booking entries) as opposed to the physical plane, over this period HEP was deemed to have to purchase that electricity from other sources. All that HEP lost in July 1998 was the contractual ability to claim electricity from the Krško NPP.

193. To the extent, if any, that ELES GEN received more than 50 percent of the electricity after 30 June 2002 and prior to 19 April 2003, it benefited insofar as it did not pay the higher spot market price for such volumes. By now complying with the 2001 Agreement as the Tribunal has interpreted it the Respondent simply transfers such "windfall" to HEP, placing it in the position foreseen for it under Article 17 and Exhibit 3. (This is virtually identical, in fact, to what was provided in Clause 17.1.2 of the 1974 Pooling Agreement [see Paragraph 82, above].) To the extent that the Respondent, rather than itself using HEP's intended share of electricity, sold same on the spot market to on-sellers to HEP,

[167] Respondent's Rejoinder, para 10

the effect of the Respondent meeting its obligations to HEP under the 2001 Agreement as interpreted by the Tribunal is, in the first instance, to transfer ELES GEN's profits on such spot market sales to HEP, thus reducing HEP's net cost of spot market purchases during the period 1 July 2002 – 19 April 2003 to the cost it would have incurred had it in fact been able to draw electricity from NEK during that period. Concededly, the Respondent will bear the additional burden of markups by the on-sellers to HEP, which would not have been incurred had Slovenia ratified the 2001 Agreement in time for it to enter into force before 1 July 2002. Whether, and, if so, to what extent, such notional burden in fact exists of course awaits further proceedings in this arbitration.

194. The point simply is that the interpretation given herein to the 2001 Agreement in no way constitutes a licence or an incentive to either party to "play games" with the ratification process. The parties' overriding concern was to re-establish the parity principle in respect of all aspects of NKK Krško. The Respondent chose to ratify when it did, rather than to renegotiate, thus necessarily accepting the consequences of that act.

THE NON-ISSUE OF RETROACTIVITY

195. As discussed extensively above, what the Claimant seeks, and the 2001 Agreement supports, is a financial adjustment equivalent to what would have been the case had the Krško NPP's electricity in fact been equally delivered to HEP and its Slovene counterpart as from 1 July 2002, as foreseen in the parties' financial settlement. For this reason, there is no issue of retroactivity on the above interpretation.

196. Nonetheless, even if there were to be an issue of retroactivity, it would clearly be resolved in HEP's favor. First it is to be noted that at the time of signature of the 2001 Agreement the obligation contained in Article 5 thereof to deliver electricity in equal parts to HEP and ELES GEN" was not something belonging to the past; it was a future, prospective obligation. The case here is not one of breach of that obligation, which clearly could not arise prior to the 2001 Agreement entering into force. Rather it is one to enforce, following entry into force of the 2001 Agreement, the financial settlement that its Article 17 and Exhibit 3 embody. Hence, this in no event would be a true case of retroactive application.[168]

197. At the time the 2001 Agreement was signed on 19 December 2001, the obligations HEP asserts under Exhibit 3 would in fact have been *prospective*; they became "retroactive" only as the treaty's entry into force became delayed. As the International Law Commission's commentary to what became VCLT Article 28 noted, retroactive application may be permitted by a "special clause" or "special object" necessitating retroactivity.[169] Such a provision was found by the Permanent Court of International Justice in the *Mavrommatis Palestine Concessions (Greece v. United Kingdom)* case.[170] In that case, Great Britain objected to jurisdiction over Greece's claims under the 1923 Protocol XII to the Treaty of Lausanne, by which Great Britain had agreed to maintain and respect the concessions granted in the Palestine trust territory by its former trustee, Turkey, before 29 October 1914, on the argument that such responsibility would be

[168] See, eg., *Ambatielos case (Greece v United Kingdom),* Jurisdiction, Judgment of 1 July, 1952 I.C.J. Rep. 28, 40 rejecting Greece's argument that it could bring a claim under a 1926 treaty based on acts which had taken place in 1922 and 1923 since there was no evidence that the 1926 treaty was intended to allow such retroactive application.

[169] *Yearbook of International Law Commission,* 1966, vol. II, para 212

[170] *P.C.I.J.* (1924) Series A, No. 2, p 34

barred by the principle of non-retroactivity of treaties. The Court rejected this argument with respect to a pre-World War I concession granted to a Greek national:

> Protocol XII was drawn up in order to fix the conditions governing the recognition and treatment by the contracting Parties of certain concessions granted by the Ottoman authorities before the conclusion of the Protocol. An essential characteristic therefore of Protocol XII is that its effects extend to legal situations dating from a time previous to its own existence. If provision were not made in the clauses of the Protocol for the protection of the rights recognized therein as against infringements before the coming into force of that instrument, the Protocol would be ineffective as regards the very period at which the rights in question are most in need of protection. The Court therefore considers that the Protocol guarantees the rights recognized in it against any violation regardless of the date at which it may have taken place.

198. Similarly, in the present case an "essential characteristic" of Exhibit 3 as interpreted by HEP is that it was intended to apply directly to a "situation" – the (non)-restoration of electricity deliveries and "parity" as of 1 July 2002 – that ended up arising before the 2001 Agreement's entry into force. Not to give effect to the agreement contemplated in this situation would be to render Exhibit 3, once it did come into force, "ineffective as regards the very period at which the rights in question are most in need of protection." On this understanding the principle of non-retroactivity would not bar HEP's claim.

199. If Slovenia's interpretation of Exhibit 3 were correct, then it still would be no clearer that VCLT Article 28 would apply. Slovenia argues that Exhibit 3 is merely a "financial settlement" containing no actual substantive or material obligations with respect to electricity deliveries to HEP, even though Slovenia acknowledged at the hearing that such deliveries were part of the intent of the 2001 Agreement. It is not clear, however, how such a liquidated financial settlement would "bind a party in relation to any act or fact which took place or any situation which ceased to exist before the date of the entry into force of the treaty." Such a settlement could be more appropriately viewed as binding the parties to the *financial* terms of that Agreement as of the date of its entry into force without, as Slovenia suggests, binding Slovenia in relation to any actual act, fact, or situation that allegedly was to occur before then.

200. Under any of the interpretations of Exhibit 3 advanced, VCLT Article 28 by its own terms clearly would not bar HEP's claim under the 2001 Agreement. The 2001 Agreement expressly stipulates the temporal applicability of Exhibit 3; under the heading "Past Financial Issues," Article 17(1) provides that:

> [m]utual financial relations *existing up to the signing of this Agreement* between NEK d.o.o., ELES d.o.o, ELES GEN d.o.o and HEP d.d. shall be regulated in accordance with the principles set forth in Exhibit 3 of this Agreement. (emphasis added)

In other words, Exhibit 3 was expressly intended to "regulate" the situation existing "up to" 19 December 2001, which date was self-evidently before either country was expected to ratify. Article 17(1) thus suggests, as is analyzed in greater detail above, that the 2001 Agreement was intended to settle the past claims on all sides existing as of the date of signature by, as Exhibit 3 provides, giving ELES six months of financial responsibility for the modernization project and six months of financial results from the Krško NPP's power generation. This express provision suffices to satisfy the intent requirement of VCLT Article 28 and thus there is no retroactivity problem here.

201. Finally as regards Article 28, it should be underscored that it, unlike Article 31, directs one not just to the text of the 2001 Agreement itself, but also permits the parties' intent of retroactivity to be "otherwise established." The very nature of the 2001 Agreement

bespeaks the parties' intention to go forward on the basis of settling the past. Incidental support for this is provided by the fact that certain steps were to be taken under the 2001 Agreement on or as of dates that clearly would precede its entry into force (For example: Article 2(3) providing "The company founders shall enter into the Memorandum of Association immediately upon the execution of this Agreement"; Exhibit 3 at (3) providing "NEK d.d. will rearrange its balance sheet on December 31, 2001"). At a minimum, to the extent any issue of retroactivity is presented, the parties' intent in that regard clearly is "otherwise established".

VII. THE DECISION

202. For all the foregoing reasons and rejecting all submissions to the contrary[171] the Tribunal DECLARES AND DECIDES as follows:

A. Pursuant to the 2001 Agreement, and in particular its Article 17(1) and its Exhibit 3 ("Principles of the Structuring of the Financial Relations"), both of which constitute integral parts of the 2001 Agreement:

(i) Declares that the aforementioned Article 17(1) and Exhibit 3 constitute a financial settlement as of 30 June 2002 between the Republic of Croatia and the Republic of Slovenia in relation to their respective companies as set forth at (ii) through (vi) hereinbelow.

(ii) Declares that the Republic of Slovenia is liable to the Claimant for the financial value to HEP of 50 percent of the electrical power produced by NEK, or by its predecessor, JP NEK, throughout the period 1 July 2002 until 19 April 2003, subject, however, to the Tribunal determining in subsequent proceedings in this arbitration whether or not, and, if so, the extent to which: (1) HEP has waived such liability by acquiescence as alleged by the Respondent (in support of which allegation the Respondent was permitted to introduce its Exhibit 326 see Paragraphs 63, 64 and 67, above); or (2) NEK or JP NEK has satisfied such liability by the offers of electrical power made to HEP by either of them on 24 June 2002 and on 13 November 2002.

(iii) Declares that HEP has waived all claims against NEK and JP NEK for damages, i.e., for compensation for undelivered electricity, i.e., for use of the capital, for any and all periods of time from the beginning of time through 30 June 2002;

(iv) Declares that NEK and JP NEK have waived all claims against HEP in connection with delivered power and electricity for any and all periods of time from the beginning of time through 30 June 2002;

(v) Declares that NEK and JP NEK have waived all claims against ELES GEN in connection with delivered power and electricity for any and all periods of time from the beginning of time through 30 June 2002;

(vi) Declares that NEK and JP NEK have waived all claims against HEP in connection with charged fees for financing of the dismantling of Krško NPP for any and all periods of time from the beginning of time through 30 June 2002; and

(vii) Declares that NEK and JP NEK have waived all claims against HEP and ELES GEN in connection with pooled resources of depreciation and in connection with the coverage of losses for any and all periods of time from the beginning of time through 30 June 2002.

[171] Having carefully considered the appended Individual Opinion of our esteemed colleague, we are, with respect, unable to agree with it.

B. Dismisses all claims asserted by HEP against the Republic of Slovenia in this arbitration as arising under the Energy Charter Treaty.

C. Reserves costs for decision in the further proceedings.

Date: [*June 12, 2009*]

[*signed*]

Mr Jan Paulsson

Arbitrator

[*signed*]

Hon. Charles N. Brower

Arbitrator

[*signed*]

Mr David A. R. Williams, Q.C.

President of the Tribunal

AGREEMENT

BETWEEN
THE GOVERNMENT OF THE REPUBLIC OF CROATIA
AND
THE GOVERNMENT OF THE REPUBLIC OF SLOVENIA

ON REGULATION OF STATUS AND OTHER LEGAL RELATIONS
REGARDING THE INVESTMENT, USE AND DISMANTLING
OF NUCLEAR POWER PLANT KRŠKO

AGREEMENT

BETWEEN

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REGARDING THE INVESTMENT, USE AND DISMANTLING

OF NUCLEAR POWER PLANT KRŠKO

(i) WHEREAS, based on the European Energy Charter, and in particular the principles established by

- the Energy Charter Treaty,
- the Convention on Nuclear Safety,
- the Joint Convention on the Safety of Spent Fuel Management and on the Safety of Radioactive Waste Management,

(ii) having a desire, as sovereign and internationally recognized states, to continue to jointly regulate their relations regarding the status, use and dismantling of Nuclear Power Plant Krško (hereinafter "NE Krško"), and

(iii) based on the Agreement, executed on October 27, 1970, between the Executive Council of the Socialist Republic of Croatia and the Executive Council of the Socialist Republic of Slovenia, ratified in the Parliament of the Socialist Republic of Croatia on December 28, 1970 ("Official Gazette" of SR Croatia No. 1/71) and in the Assembly of the Socialist Republic of Slovenia on December 10, 1970 ("Official Gazette" of SR Slovenia No. 44/70),

(iv) taking into account the Agreement on the pooling of resources for joint construction and exploitation of NE Krško, executed on March 22, 1974, between Elektroprivreda Zagreb and Savskih elektrarn Ljubljana, and the respective Annex dated as of April 16, 1982,

(v) taking into account the Self-Management Agreement on regulation of mutual rights and liabilities between the founders and NE Krško, executed on April 16, 1982 between ZEOH Zagreb and EGS Maribor, and

(vi) taking into account the Agreement on preparing the construction of a second joint croatian-slovenian nuclear power plant, executed on April 21, 1985 between ZEOH Zagreb and EGS Maribor,

(vii) taking into account that NE Krško investors were entered into the court register of the Regional Court Novo Mesto under No. 56/84 of February 29, 1984 as the founders,

the Government of the Republic of Croatia and the Government of the Republic of Slovenia (hereinafter: the Contracting Parties) agree as follows:

Article 1

(Legal Successors)

(1) The Contracting Parties confirm that NE Krško was built with the funds of Croatian and Slovenian electrical power companies, represented on the Croatian side by Elektroprivreda Zagreb, and on the Slovenian side by Savske elektrarne Ljubljana. The legal successor of the Croatian electrical power companies' rights and obligations arising from the construction and use of NE Krško is Hrvatska elektroprivreda d.d. Zagreb (hereinafter: HEP d.d), and the legal successor of the Slovenian electrical power companies is ELES GEN d.o.o. Ljubljana.

(2) The funds required for the construction of the nuclear power plant were invested in equal parts, based on the proceedings listed in the preamble hereto, by the investors, i.e. by their legal successors, who, as a result, acquired the basis for acquiring the Shareholder rights in NE Krško in accordance with this Agreement.

(3) The Contracting Parties agree that the legal successors of the investors from both Contracting Parties exercise their rights and obligations regarding the management and use of jointly owned NE Krško in equal parts and in equal proportions, unless otherwise established in this Agreement.

Article 2

(NEK d.o.o. Company)

(1) The Contracting Parties agree that the existing Javno poduzeće Nuklearna elektrana Krško, a limited liability company (JPNEK d.o.o.), as transformed by the Decree of the Government of the Republic of Slovenia of July 30, 1998, from Nuklearna elektrana Krško p.o., is to be transformed into Nuklearna elektrana Krško, Limited liability company (hereinafter: Company or NEK d.o.o.), in accordance with this Agreement and the respective Memorandum of Association which shall be entered into, based on this Agreement, between Hrvatska elektroprivreda d.d. Zagreb and ELES GEN d.o.o. Ljubljana (hereinafter: company founders or Shareholders).

(2) The Company operates based on the principle of covering of all expenses, and therefore in principle does not produce either losses or profits as a result of its operation.

(3) The agreement being entered into by the company founders (hereinafter Memorandum of Association) shall be based on the provisions of this Agreement and on the provisions of the Commercial Companies Act of the Republic of Slovenia. The Contracting Parties shall ensure that the company founders enter into a Memorandum of Association substantially in the form enclosed in exhibit 1 of this Agreement. The company founders shall enter into the Memorandum of Association immediately upon the execution of this Agreement, provided the Memorandum of Association shall enter into force simultaneously with entry into force of this Agreement. The Memorandum of Association is considered the founding document of the company, and does have to be notarized in

accordance with the Commercial Company Act to be legally valid. The executed Memorandum of Association is not an integral part of this Agreement.

(4) The base capital of NEK d.o.o. is 84.723,482.000,00 SIT (eighty-four billion seven hundred twenty-three million four hundred eighty-two thousand Slovenian Tolars).

(5) The base capital of NEK d.o.o. is divided into two equal parts owned by Hrvatska elektroprivreda d.d. Zagreb and ELES GEN d.o.o. Ljubljana.

(6) Decisions on withdrawal or dismissal of a Shareholder from the company, and the decisions on premature liquidation of the company require the consent of the Contracting Parties.

(7) The Contracting Parties agree not to act in a manner which might revoke or restrict the rights of Shareholders.

Article 3

(Company Bodies)

(1) The Company bodies are the Shareholders' Assembly, the Supervisory Board and the Management Board, all of which are composed on a parity basis, unless agreed to otherwise in this Agreement.

(2) The Slovenian member is entitled to make a recommendation for the Chairman of the Management Board, and the Croatian member is entitled to make a recommendation for the Vice-Chairman of the Management Board. If a consensus cannot be reached within a parity composed Management Board, the vote of the Chairman of the Management Board will be the deciding vote (hereinafter: casting vote). The casting vote of the Chairman of the Management Board is used only in exceptional circumstances, and only when the failure to reach consensus in the Management Board might jeopardize the safety of the plant operation, substantially jeopardize achievement of goals determined by the adopted annual plan or cause significant damages to the company.

(3) In the case of the Chairman of the Management Board using the casting vote, he must immediately request the Chairman of the Supervisory Board to convene the meeting of the Supervisory Board during which the justifiableness of the use of the casting vote shall be reviewed and appropriate decisions adopted.

(4) When the casting vote is used, the members of the Management Board who voted against the decision are not liable for damages which might arise from such decision of the Chairman of the Management Board.

(5) The Croatian Shareholder is entitled to make a recommendation for the Chairman of the Supervisory Board, and the Slovenian Shareholder is entitled to make a recommendation for the Vice-Chairman of the Supervisory Board.

(6) The representatives of the employees of NEK d.o.o. (wider organization) are entitled to participate in the meetings and decisions of the Supervisory Board, but only when legal-

employment issues related to NEK d.o.o. employees are being directly discussed and decided upon. In such cases, the Supervisory Board consists of three parts, an equal number of Slovenian Shareholder representatives, Croatian Shareholder representatives and of NEK d.o.o. employee representatives, which were appointed in accordance with regulations governing the employees' participation in the management. The specific provisions governing the structure and operation of the Supervisory Board in the wider organization are provided in the Memorandum of Association.

(7) The Contracting Parties agree that the Slovenian regulations regarding employees' participation in management pertaining to an employee director shall not be applicable to NEK d.o.o.

(8) The Shareholders' Assembly shall appoint the recommended members of the Management Board and the Supervisory Board, if they were recommended in accordance with this Agreement and the Memorandum of Association.

(9) The Contracting Parties agree that the issues which cannot be decided upon by the company bodies due to the parity composition, shall be resolved by a business arbitration, whose award shall be final and binding on the Company. The provisions regarding the structure, competence and operation of such arbitration are provided in the Memorandum of Association.

Article 4

(Duration, Right of First Refusal)

(1) NEK d.o.o. is incorporated for a definite term, i.e. until the end of the process of dismantling of the nuclear power plant.

(2) During any eventual sale of the real property of NEK d.o.o., the Republic of Slovenia, i.e. the legal person authorized by it in accordance with Exhibit 2 hereof, has the right of first refusal. Such right of first refusal has priority over other legal rights of first refusal.

Article 5

(Production and Transmission)

(1) The Contracting Parties agree that NE Krško is a significant electric power resource for the electric power systems of both countries, and the Contracting Parties are extremely interested in the safe operation of this power plant.

(2) The Contracting Parties agree that the Company shall deliver the produced power and electricity to the Shareholders in equal proportions, half to each Shareholder, until the end of the regular useful life of the nuclear power plant in the year 2023, i.e. until the extended useful life of the power plant, if approved (hereinafter: useful life).

(3) The Contracting Parties agree that the delivery of the generated electric power shall be done in compliance with European norms, under equal terms for both Shareholders.

(4) The operator of the transmission network from the Republic of Slovenia shall provide to the Shareholder from the Republic of Croatia the transmission of power and electricity from Paragraph 2 of this Article, by the shortest transmission route. The Shareholder from the Republic of Croatia must accept the delivered electricity. For the transmission of the power and electricity from NE Krško the operator of the transmission network shall charge the Shareholders from the Republic of Croatia the transmission costs in accordance with the existing and international practices.

(5) The legal entities in the Republic of Croatia and in the Republic of Slovenia authorized to manage the electric power systems and transmission of electric power and NEK d.o.o. shall regulate their relations by a separate agreement, as needed.

(6) The available power and generated electricity which has been delivered according to Paragraph 2 of this Article and transmitted according to Paragraph 4 of this Article is free of customs and other duties.

(7) The Slovenian electricity market regulations shall not apply to the electricity generated in NE Krško, which is, according to Paragraph 2 of this Article, accepted by the Shareholder from the Republic of Croatia.

Article 6

(Price, Expenses)

(1) The Shareholders shall pay the delivered power and electricity at the price covering the full operating costs, including, *inter alia*, the depreciation costs, in the amount necessary for achieving the long-term investment renewal and investment in technical improvements regarding the safety and economic efficiency of the nuclear power plant. The set provisional price for the power and electricity is established based on annual budget in accordance with the elements set forth in the Memorandum of Association. At the end of the business year a calculation shall be performed according to electricity actually generated and actual operating costs.

(2) In case when the nuclear power plant is not operating due to causes which cannot be attributed to any of the Contracting Parties, i.e. to neither of the Shareholders, and when the cause of such event is outside the plant and could not be foreseen, and its consequences could not have been avoided or remedied (Force Majeure), i.e. due to a cause which could not have been foreseen, and the consequences could not have been avoided or remedied (occurrence), both Shareholders shall jointly cover the expenses incurred in equal proportions.

(3) The actions of state or local authorities, except for actions which relate to nuclear safety, are not considered to be events of Force Majeure.

(4) If the circumstances from Paragraph 2 of this Article are continuing longer than 12 months, and the Shareholders do not agree otherwise, the procedure of premature closing down of NE Krško shall be performed.

(5) The Shareholders shall regularly perform their financial duties towards NEK d.o.o. and guarantee their payment obligations.

(6) NEK d.o.o. may terminate the delivery of electric power to the Shareholder who continually fails to perform its obligations, i.e. who fails to provide the appropriate guarantee for the payment of its obligations.

Article 7

(Extraordinary Expenses)

The Contracting Parties shall take the appropriate measures to ensure that the Shareholders in principle provide the funds for the payment of extraordinary expenses and for new investments into NE Krško in equal proportions, unless such funds are provided from the price set forth in Paragraph 1 of Article 6 hereof.

Article 8

(Employment, Education)

(1) The Contracting Parties agree that the Memorandum of Association will determine the obligation of NEK d.o.o. to apply the parity principle in employment for the members of the Management Board and for other employees with special authority as defined in the Memorandum of Association.

(2) The Company shall define those job positions for which free employment shall be secured, taking into account the principles of safety, optimal operation of the nuclear power plant and appropriate representation of experts from both Contracting Parties.

(3) The Republic of Slovenia undertakes, in compliance with Paragraph 1 and Paragraph 2 of this Article, and upon recommendation by the Company, to enable free employment to those persons who have the status of a legal alien.

(4) In education, scholarship awards and professional training, NEK d.o.o. shall be governed by the principle of equal rights, regardless of nationality.

(5) The provisions of this Article shall also apply to those persons who are already employed by NEK d.o.o.

Article 9

(Contractors)

(1) The Contracting Parties agree that, for the needs of the regular operation as well as in extraordinary situations, NEK d.o.o. shall ensure the participation of companies and institutions that comply with the requirements for qualified contractors in nuclear power plants. In addition to complying with the above-mentioned condition as well as the

requirement of competitiveness, NEK d.o.o. shall ensure the participation of the suppliers and contractors equally from both Contracting Parties.

(2) The Contracting Parties agree to treat the suppliers and contractors of NEK d.o.o. from the states of both Contracting Parties equally in all respects.

Article 10

(Dismantling, Radioactive Waste and Spent Nuclear Fuel)

(1) The dismantling of NE Krško, the disposal of radioactive waste and spent nuclear fuel, as established in the Joint Convention of the preamble of this Agreement, is a joint liability of both Contracting Parties.

(2) The Contracting Parties agree to ensure an effective joint solution for the dismantling and the disposal of radioactive waste and spent nuclear fuel, both economically and environmentally.

(3) The disposal of radioactive waste and spent nuclear fuel from the plant and the dismantling shall be performed pursuant to the Program of disposal of radioactive waste and spent nuclear fuel (hereinafter: Program of disposal of RW and SNF). The Program of disposal of RW and SNF shall be prepared in cooperation with NEK d.o.o, in compliance with international standards by expert institutions, which the Contracting Parties shall determine within 60 days from the date of entry into force of this Agreement. The Program of disposal of RW and SNF, *inter alia*, includes the following: the proposal of possible division and takeover of radioactive waste and spent nuclear fuel, the criteria of acceptability for disposal and assessment of the required financing and terms of performance. The Program of disposal of RW and SNF shall be prepared within 12 months from the date of entry into force of this Agreement, and shall be verified by the bilateral committee as set forth in Article 18 hereof. The Program of disposal of RW and SNF shall be reviewed at least every five years.

(4) The dismantling will be implemented in compliance with the Dismantling Program. The Dismantling Program shall include the disposal of all radioactive and other waste resulting from the dismantling until the removal from the location of NE Krško, assessment of required financing and the terms of its implementation.

(5) The Dismantling Program shall be prepared by expert institutions from Paragraph 3 of this Article, together with NEK d.o.o., and in accordance with the international standards, within 12 months at the latest from the date of entry into force hereof. The Dismantling Program shall be verified by the bilateral committee form Article 18 hereof, and shall be approved by the administrative body of the Republic of Slovenia competent for the nuclear safety. The Dismantling Program shall be reviewed at least every five years.

(6) The site of NE Krško may be used for a temporary disposal of radioactive waste and spent nuclear fuel until the end of its useful life.

(7) Should the Contracting Parties fail to reach an agreement on a joint solution of disposal of radioactive waste and spent nuclear fuel by the end of the regular useful life, the

Contracting Parties undertake that they shall no later than two years from that time complete the takeover and removal of radioactive waste and spent nuclear fuel from the NE Krško site in equal proportions. Further takeover and removal shall be done in accordance with the Program of disposal of RW and SNF and Dismantling Program, at least every five years, unless the approved programs provide otherwise.

(8) If the premature closing down of NE Krško occurs pursuant to action of the government of the Republic of Slovenia, which is not a consequence of Force Majeure or an occurrence set forth in Article 6 hereof, the Republic of Croatia shall participate in the dismantling and the disposal of radioactive waste and spent nuclear fuel in a proportion equal to the ratio of the electricity which was actually taken over by the Shareholder from the Republic of Croatia as compared to the electricity which NE Krško would have generated under normal circumstances from the beginning of its operation until the end of its useful life.

Article 11

(Financing of Dismantling and Disposal)

(1) The Contracting Parties undertake to secure in equal proportions the financing of the costs of preparing the Dismantling Program, the costs of its implementation and the costs of preparing the Program of disposal of RW and SNF.

(2) If the Contracting Parties agree on a joint solution for the disposal of radioactive waste and spent nuclear fuel, those expenses shall also be financed in equal proportions. If such an agreement is not reached, the Contracting Parties shall independently bear the costs of all activities relating to implementation of the Program of disposal of RW and SNF which are not of joint character.

(3) The Contracting Parties shall, within 12 months from the date of entry into force hereof, adopt the appropriate regulations for provision of resources for financing of expenses from Paragraphs 1 and 2 of this Article, so that each Contracting Party shall provide regular payments into its separate fund in the amount required by the approved programs from Article 10 hereof. The Contracting Parties, i.e. their separate funds will finance in equal proportions all activities regarding the dismantling and disposal of radioactive waste and spent nuclear fuel created during the operation and dismantling of NE Krško that are approved by the bilateral committee in Article 18 hereof.

(4) In the event of occurrence of circumstances from Paragraph 8 of the Article 10 hereof, the financing of expenses from Paragraphs 1, 2 and 3 of this Article, which the Contracting Parties would otherwise bear in equal proportions, shall be appropriately changed.

(5) Each of the Contracting Parties jointly guarantees the liabilities of its separate fund.

(6) The Contracting Parties will regularly inform each other of the amount of collected funds in their separate funds.

(7) Pursuant to the Dismantling Program, the dismantling of NE Krško shall be performed by NEK d.o.o.

Article 12

(Protection of Investments)

(1) The Contracting Parties agree:

1. that the exercise of the rights of the Shareholders arising from this Agreement cannot be limited, neither temporarily nor permanently;

2. that they shall ensure fair and impartial treatment of the Shareholders belonging to the other Contracting Party on their territories, i.e. that they shall treat such Shareholder the same way as its own Shareholder, with full protection and security of investments for the duration of the joint investment.

(2) The Contracting Parties undertake that they shall not encumber the production and assumption of electricity from NEK d.o.o. by any public taxes imposed by the state or the local authorities which were not in force at the time of the execution of this Agreement, and which refer to NE Krško as a nuclear facility, i.e. that the existing public taxes shall not be actually increased. For other public taxes, the Republic of Slovenia warrants that NEK d.o.o. shall be treated the same as other legal persons in the Republic of Slovenia.

(3) If a grant of an appropriate concession is determined for the generation of the electricity, the Republic of Slovenia undertakes to grant such a concession free of charge to NEK d.o.o. for the duration of the useful life of the nuclear power plant.

Article 13

(Protection against Expropriation)

(1) The investments of the Shareholder from the Republic of Croatia cannot be expropriated, nor can any other measures be taken against it which have the same effect as expropriation (hereinafter: expropriation), unless the measure in question is in the public interest with respect to internal needs of the Republic of Slovenia, and is implemented on a non-discriminatory basis and with prompt, appropriate and effective compensation.

(2) Compensation for expropriation is determined in accordance with Article 13 of the Energy Charter Treaty while giving effect to Article 16 of the International Accounting Standards.

(3) The provisions of the above Paragraphs shall apply equally to revenues from investments and to partial or full liquidation.

Article 14

(Repatriation of Investments and Revenues)

The Republic of Slovenia guarantees to the Shareholder from the Republic of Croatia, after the settlement of tax dues, an unlimited transfer of its investments, revenues and earnings of

the Croatian nationals employed at NE Krško d.o.o. The transfers shall be performed without delay in convertible currency. The transfers shall be effected according to the exchange rate applicable on the date of the transfer, subject to valid foreign currency regulations and in accordance with the same treatment applicable to the repatriation of the investments and revenues of investors from third countries.

Article 15

(Subrogation)

(1) If a Contracting Party or its appointed legal entity makes a payment pursuant to a claim for damages, a warranty or an insurance agreement related to the investment, the other Contracting Party shall recognize the transfer of all rights or claims of the injured Shareholder to the first Contracting Party or its appointed legal entity. The first Contracting Party or its appointed legal entity has the authority to exercise such rights and enforce such claims to the same extent as the Shareholder itself based on subrogation.

(2) The first Contracting Party or its appointed legal entity is always entitled to equal treatment in connection with the rights or the claims realized as a result of the transfer.

Article 16

(Impact on Environment)

The Contracting Parties commit to regularly inform each other about the impact of NE Krško on the environment.

Article 17

(Past Financial Issues)

(1) Mutual financial relations existing up to the signing of this Agreement between NEK d.o.o., ELES d.o.o., ELES GEN d.o.o. and HEP d.d. shall be regulated in accordance with the principles set forth in Exhibit 3 of this Agreement.

(2) The Contracting Parties agree that, as of the date of entry into force hereof, all obligations of NEK d.o.o. to the Fund for financing the dismantling of NE Krško and disposal of radioactive waste from NE Krško, which obligations arose from the application of the Act on Fund for Financing of Dismantling of NE Krško and Disposal of Radioactive Waste from NE Krško ("Official Gazette" of the Republic of Slovenia No. 75/94), shall cease to exist.

Article 18

(Bilateral Committee)

(1) The Contracting Parties shall establish a bilateral committee which will monitor the implementation of this Agreement and perform other tasks in accordance with this

Agreement. The committee consists of the delegations of the Contracting Parties. Each delegation has a chairman and four members.

(2) The committee shall rotate the location of its meetings between the territories of the two Contracting Party. The first meeting shall be convened by the chairman of the Slovenian delegation within 90 days from the date of entry into force of this Agreement.

(3) The Rules of Procedure of the bilateral committee are provided in Exhibit 4 of this Agreement and are not considered an integral part of this Agreement.

Article 19

(Dispute Resolution)

(1) All disputes between one Contracting Party and the members of the Company from the other Contracting Party shall be resolved amicably and in good faith in the first instance.

(2) If a dispute cannot be settled amicably within six months from the date of written report to the other Contracting Party, the aggrieved Shareholder may, at its discretion, refer the dispute for resolution to:

a) a court of competent jurisdiction of the aggrieved Contracting Party;

b) to ad hoc arbitration in accordance with the Arbitration Rules of Procedure of the United Nations Commission for International Law - UNCITRAL;

c) an arbitration court in accordance with the rules of the Arbitration Institute of the Stockholm Chamber of Commerce;

d) the Arbitration Court of the International Arbitration Center of the Federal Chamber of Commerce in Vienna;

e) the International Centre for Settlement of Investment Disputes - ICSID - in accordance with the Convention on the Settlement of Investment Disputes between States and Nationals of Other States and the additional contract on regulation of Conciliation, Arbitration and Fact-finding.

(3) The decision shall be final and binding. Each of the Contracting Parties shall ensure the acknowledgement and enforcement of the arbitration award in accordance with its legislation.

Article 20

(Dispute Resolution)

(1) Any disputes between the Contracting Parties which arise out of or in connection with the interpretation or application of this Contract, shall be settled in the first instance by negotiation.

(2) If a dispute under paragraph 1 of this Article cannot be resolved within six months, upon request of one of the Contracting Parties, the dispute shall be referred to an arbitration court.

(3) Such arbitration court shall be formed ad hoc as follows: each of the Contracting Parties shall appoint one arbitrator, and those two arbitrators shall agree on the choice of a

national of a third state who will chair the arbitration court. Those arbitrators shall be appointed within two months of the date one of the Contracting Parties notified the other of its intention to refer the dispute to an arbitration court. The chairman of the court shall be appointed within two months.

(4) If the terms stated in paragraph 3 of this Article are not complied with, any of the Contracting Parties may, in the absence of another relevant agreement, call on the chairman of the International Court of Arbitration in Hague (hereinafter: International Court) to make the necessary appointments. If the chairman of the International Court is a national of one of the Contracting Parties or is otherwise prevented in performing the said duty, the vice-chairman, or in case of his unavailability, the next in rank member of the International Court, shall be called upon to perform the necessary appointments under same conditions.

(5) The arbitration court will establish its own rules of procedure.

(6) The arbitration court shall reach a decision on the basis of this Agreement and in accordance with the rules of the international law. The arbitration court shall reach a decision by a majority of votes. The decision is final and binding.

(7) Each of the Contracting Parties shall bear its member's costs and the costs of its representation in the arbitration proceedings before the court. The costs of the arbitration chairman and other costs shall be borne by both Contracting Parties in equal proportions. The Arbitration court, however, may, in its decision, determine a different allocation of costs.

Article 21

(Registration of the Agreement)

This Agreement, after entry into force, shall be registered with the United Nations in accordance with the Article 102 of the United Nations Charter. The registration shall be carried out by the Republic of Slovenia.

Article 22

(Closing Provisions)

(1) By entry into force of this Agreement, the provisions of the Agreement executed on October 27, 1970, between the Executive Council of Socialist republic of Croatia and the Executive Council of the Socialist Republic of Slovenia, as ratified in the Parliament of the Socialist Republic of Croatia on December 28, 1970 and in the Assembly of the Socialist Republic of Slovenia on December 10, 1970, shall cease to have effect.

(2) All other issues which are not stipulated herein shall be governed by the Agreement between the Government of the Republic of Croatia and the Government of the Republic of Slovenia on stimulation and mutual protection of investments.

(3) This Agreement shall be ratified by the Croatian Parliament, i.e. in the Parliament of the Republic of Slovenia.

(4) This Agreement shall enter into force on the date of receipt of the last written diplomatic notice that all conditions as required by the legislations of the Contracting Parties required for its entry into force have been complied with.

This Agreement is executed in Krško, on 19 December 2001, in two originals in Croatian and Slovene languages, and both language versions are equally valid.

FOR THE GOVERNMENT OF THE REPUBLIC OF CROATIA	FOR THE GOVERNMENT OF THE REPUBLIC OF SLOVENIA
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EXHIBIT 1

NEK d.o.o.

MEMORANDUM OF ASSOCIATION

5 July 2001

Pursuant to the Agreement between the Government of the Republic of Croatia and the Government of the Republic of Slovenia on regulation of status and other legal relations regarding the investment, use and dismantling of Nuclear Power Plant Krško, and Article 409 of the Companies Act ("Official Gazette" of the Republic of Slovenia Nos. 30/93, 29/94, 82/94, 20/98, 6/99 and 45/01), the legal successors of the Nuclear Power Plant Krško founders, being

HRVATSKA ELEKTROPRIVREDA d.d., Ulica grada Vukovara 37, 10000 Zagreb, Republic of Croatia, represented by the chairman of the board, Mr. Ivo Čović, as the legal successor of the Nuclear Power Plant Krško founders from the Republic of Croatia,

and

ELES GEN d.o.o., Hajdrihova 2, Ljubljana, Republic of Slovenia, represented by its director, Mr. Vekoslav Korožec, as the legal successor of the Nuclear Power Plant Krško founders from the Republic of Slovenia

executed on this day of 19.12.2001, in Krško, the following

MEMORANDUM OF ASSOCIATION

Introduction

Article 1

1.1. It is agreed that an Agreement has been entered into between the Government of the Republic of Croatia and the Government of the Republic of Slovenia on regulation of status and other legal relations regarding the investment, use and dismantling of Nuclear Power Plant Krško (hereinafter: the Bilateral Agreement), whereby the signatories to the agreement established their mutual relations regarding the status, use and dismantling of NE Krško, after the declaration of independence of both countries and the establishment of new socio-political and economic systems in both Contracting Parties.

1.2. It is agreed that, as set forth in Article 2 of the Bilateral Agreement, the Contracting Parties to this Memorandum of Association are the legal successors to the original investors and founders of the existing NE Krško from both signatories to the Bilateral Agreement which successors must continue to exercise their rights and obligations regarding the management and the use of the joint NE Krško.

1.3. It is agreed that the existing legal status of NEK d.o.o. is a limited liability company, registered under No. 1/00120/00 in the court register at the District Court in Krško.

Article 2

2.1. The Contracting Parties agree that, based on Article 2 of the Bilateral Agreement, the existing Javno poduzeće NE Krško d.o.o. is transformed into NE KRŠKO d.o.o. (hereinafter: the Company), in accordance with the provisions of the Bilateral Agreement and the Commercial Companies Act ("Official Gazette" of the Republic of Slovenia Nos. 30/93, 29/94, 82/94, 20/98, 6/99 and 45/01 – hereinafter: the CCA).

2.2. Based on this Memorandum of Association, the Contracting Parties, as the legal successors of the original joint NE Krško investors, as set forth in Article 2 of the Bilateral Agreement, become the founders and Shareholders of the Company who agree that the newly established Company is the legal successor of all rights and obligations of the joint NE Krško in its existing legal status.

Article 3

3.1. This Memorandum of Association is based on the provisions of the Bilateral Agreement and the provisions of the CCA.

3.2. Whenever the mutual relations are not otherwise regulated by the Bilateral Agreement and the Memorandum of Association, relevant provisions of the Bilateral Agreement and the CCA shall apply to the mutual relations between the founders and Company Shareholders, the relations between the founders and the Company Shareholders and the legal status of the Company in legal transactions.

Article 4

This Memorandum of Association is the highest act of the Company. Any other acts adopted by the Company bodies in accordance with this Memorandum of Association shall not be in conflict with the provisions of this Memorandum of Association.

Name and Registered Office of the Company

Article 5

5.1. The Company has the following name: Nuklearna elektrana Krško d.o.o.

The abbreviated name of the Company is: NEK d.o.o.

The registered office of the Company is in Krško, Vrbina 12, Slovenia.

5.2. The Company name translated into English is: Nuclear Power Plant Krško d.o.o.

The Company name translated into a foreign language shall be used only in conjunction with the Company name in the Slovenian language.

5.3. The form and substance of the Company logo, used by the Company in legal transactions, shall be decided upon by the Company Supervisory Board.

Company objective and term

Article 6

6.1. It is agreed that the objective of the Company is the generation and distribution of electricity exclusively for the benefit of the Shareholders. Pursuant to the above, the Company may not produce and distribute electricity to third parties except with the consent of both Shareholders, and except as provided herein.

6.2. The Company is created for a definite term, i.e. until the end of the procedure of dismantling of the nuclear power plant.

6.3. Upon expiration of the term of the Company, the Company will be liquidated in accordance with applicable regulations. As to the sale of the Company's real property, the Republic of Slovenia, or a legal person duly authorized on its behalf, has the right of first refusal in accordance with the provisions of the Bilateral Agreement.

Scope of business

Article 7

The Company performs economic activities within the scope of activities it is registered for.

In accordance with the Standard Classification of Activities, the Company's activities are as follows:

- E/40.102 Generation of electricity in thermal and nuclear power stations
- K/74.204 Miscellaneous planning and technical advice
- K/74.30 Technical testing and analysis
- K/73.102 Technological research and experimental development

The Company may perform, without registration, other activities whose purpose is to perform the registered activities, which are usually performed in conjunction with such activities in limited scope or from time to time, or which contribute to a more complete utilization of capacities that are being used to perform said activities.

Representation

Article 8

The Company shall be represented by persons duly authorized for such representation in accordance with Articles 9 and 34 hereof and a special resolution adopted by the Shareholders' Assembly.

Authorized Agents

Article 9

9.1. The Company may appoint one or more authorized agents, who will be authorized on its behalf to perform all legal actions within the legal capacity of the Company, except for the alienation and encumbrance of the real property of the Company for which authorized agents must obtain an authorizing resolution from the Shareholders' Assembly.

9.2. Any decision on assignment of authority to respective authorized agents shall be made by the Shareholders' Assembly.

9.3. The Company and the authorized agents shall enter into a special agreement with regards to their mutual relations.

Company property, capital and business shares

Article 10

10.1. The Company capital is SIT 84,723,482,000.00 (eighty-four billion seven hundred twenty-three million four hundred eighty-two thousand Slovenian Tolars).

10.2. Upon the execution of this Memorandum of Association, the capital shall be deemed to have been fully invested into the Company.

Article 11

11.1. The Shareholders' initial contributions to the capital, as set forth in the preceding article, are as follows:

1. Hrvatska elektroprivreda d.d. Zagreb has made an initial contribution in the amount of SIT 42,361,741,000.00 (forty-two billion three hundred sixty-one million seven hundred forty-one thousand Slovenian Tolars),
2. ELES GEN d.o.o. Ljubljana has made an initial contribution in the amount of SIT 42,361,741,000.00 (forty-two billion three hundred sixty-one million seven hundred forty-one thousand Slovenian Tolars).

11.2. The Shareholders acquire their business shares according to the specific initial capital contributions.

11.3. The rights arising from the business shares are equal, unless otherwise specified in this Memorandum of Association.

Transfer of business shares

Article 12

12.1. Any free or chargeable use of business shares between the Shareholders and among the Shareholders and third parties is considered the transfer of business shares under this Memorandum of Association.

12.2. The transfer of business shares between the Shareholders is not restricted.

12.3. Any transfer of business shares to third parties that have a status of subsidiaries in which a Shareholder has a majority interest, that is, the majority management rights, or any transfer to third persons in which the Contracting Parties to the Bilateral Agreement have a majority interest or the majority management rights, is also unrestricted.

12.4. Any transfer of business shares which occurs as a result of Shareholders' legal status changes shall not be regarded as a transfer of business shares under paragraph 1 of this Article; consequently, a transfer of business shares from Shareholders to legal

successors resulting from such statutory changes shall not be regarded as such a transfer.

Article 13

A Shareholder shall not transfer its business share to third persons without an explicit written approval of the other Shareholder.

Article 14

Partition of business shares is not allowed.

Encumbrance of a business share

Article 15

15.1. A Shareholder shall not encumber its business share with a lien or some other material right without an explicit written approval of the other Shareholder.

15.2. A Shareholder shall immediately notify the other Shareholder in case of a third party having initiated proceedings against a business share.

Increase of Initial Capital

Article 16

16.1. Based on decisions made by the Shareholders' Assembly with regard to increase of the initial capital, Shareholders may register new contributions by making payments, i.e. in monies and in kind (effective increase of the initial capital).

16.2. Based on decisions made by the Shareholders' Assembly, the initial capital may also be increased by transfer of the Company reserves, i.e. the profits (nominal increase of the initial capital).

16.3. Above listed means of increasing the initial capital may be carried out only if the business share ratio of 50%:50% is retained during the increase, in accordance with Article 11 Paragraph 2 of this agreement.

Article 17

Statements regarding the assumption of a new initial contribution must be notarized.

Article 18

18.1. If the initial capital is increased by input in kind, the scope and value of contribution shall be determined by a decision on the increase of the initial capital. The

value of the contribution shall be determined by a certified estimator appointed by the Shareholders' Assembly.

18.2. Prior to submission of the application for registering the increase of the initial capital in the court register, the Shareholder providing the input in kind must enter into a relevant agreement with the Company on the transfer of the matter, i.e. the rights, to the Company.

Article 19

19.1. Under the effective increase of the initial capital, the Shareholders shall pay, i.e. input, and assume, new contributions according to the ratio of their existing initial contributions in the initial capital of the Company.

19.2. Under the nominal increase of the initial capital, the new contributions shall be assumed by the previous Shareholders proportionally to their existing initial contributions in the initial capital of the Company, in such a way that the overall ratio of initial contributions of the Shareholders in the initial capital remains unchanged.

Reduction of initial capital

Article 20

20.1. The initial capital may be reduced pursuant to a resolution of the Company Shareholders' Assembly. Any resolution on reduction of the initial capital must include the scope and purpose of the reduction of the initial capital, as well as the manner and the conditions of implementing the reduction.

20.2. Any reduction in the value of the initial capital, as set forth herein, such as reduction caused by the return of the initial contributions to the Shareholders, reduction caused by lowering of the nominal amount of the Shareholders' contributions and the withdrawal of business shares, shall be considered a reduction of the initial capital.

Article 21

Every reduction of the initial capital shall be made in compliance with the law.

Article 22

A reduction of the initial capital is valid if the following conditions are met:

- if the Management Board has on two separate occasions issued a notice of the decision to reduce the initial capital, in which notice it invited the Company creditors to contact the Company and state whether they consent to the reduction of the initial capital, provided that the Company must directly notify those creditors which are known to the Company;

- if the Company fulfills the requirements of creditors who do not agree with the initial capital reduction, that is, if it furnishes them with appropriate insurance provisions.

Withdrawal of business share

Article 23

Withdrawal and/or exclusion from the Company shall be allowed only with the relevant consent of the Republic of Croatia and the Republic of Slovenia.

Article 24

24.1. The Shareholder whose business share is being withdrawn pursuant to the preceding Article shall be entitled only to the disbursement of the monetary value of the initial capital as of the date of withdrawal. For the purposes of evaluation of the value of contribution in case of withdrawal of one of the Shareholders, the evaluation shall be made by authorized auditors appointed by the Company Supervisory Board. The evaluation shall be made on the day of withdrawal at the expense of the Company. The Company shall disburse the withdrawing Shareholder the amount of the contribution within 6 (six) years from the date of the withdrawal, with interest at the rate payable by banks for demand deposits.

24.2. The act of withdrawal from the Company shall terminate the business share of the Shareholder, as well as all rights and obligations the Shareholder used to exercise in relation to the business share.

Relations between Shareholders with regard to exploitation of NE Krško

Article 25

25.1. These provisions regulate the right to utilize the power and energy produced in NE Krško within the scope of activities set forth in Article 7.

25.2. Each Shareholder has the right and obligation to purchase 50% (fifty percent) of the total available power and electricity generated at NE Krško in accordance with this Memorandum of Association.

25.3. Should Shareholders fail to use in entirety their respective parts of the total available power (50%), they will bear the expenses as if they used their respective parts in their entirety.

Article 26

Generation of electricity within the available power for each consecutive year shall be agreed upon by the Shareholders and the Company by means of an annual budget, which shall, *inter alia*, include an annual generation budget and an annual expense budget. The annual budget shall be adopted by the Company Supervisory Board following recommendations made by the Management Board. If the Company Supervisory Board fails to adopt an annual budget for the next year by December 31 of the current year, the annual generation budget shall be determined independently by the Management Board.

Price of power and electricity from NEK

Article 27

27.1. Provisional prices for the available power and electricity for each business year shall be established by the Company in advance.

27.2. Any such price set shall be established by the Management Board, with the consent of the Supervisory Board, not later than October 1 for the following year. If consensus cannot be reached, the latest provisional price is effective, multiplied by the coefficient of the increase in basic living costs in the Republic of Slovenia since the provisional price was last established.

27.3. The provisional price of the available power and electricity from the nuclear power plant shall be established based on the annual budget, which consists of the expense budget and generation budget, as well as the long-term investment plan, so that such price covers all operating costs of the Company.

Article 28

28.1. The elements of the expense budget and the price determination are primarily the following:

- nuclear fuel costs and other costs pertaining to such fuel,
- water dues,
- costs of materials and services,
- depreciation up to the amount required for new investments and the principal repayment of investment credits for such investments, all established by the long-term investment plan,
- insurance premiums,
- land use charges and other obligations to the local community,
- operating costs,
- operating asset write-offs,
- interest costs and other financing expenditures, and
- taxes and other operating expenditures.

28.2. The Company shall charge:

- the available generated power of the nuclear power plant in 12 monthly payments,
- the active power per number of net generated kWh of NEK at the negotiated price in 12 monthly payments.

Article 29

At the end of the year, prior to the balance sheet preparation, business results shall be determined and calculations made in a manner that will allow the price for the distributed power and energy to cover all costs and expenditures incurred by the Company.

Article 30

30.1. The Shareholders undertake to meet their obligations toward NEK d.o.o. within 15 days from the date of issue of each respective invoice. For any overdue payment NEK d.o.o. shall charge interest enforceable for sales contracts in the Republic of Slovenia.

30.2. To ensure payment of invoices, the Shareholders shall furnish to the Company, within 3 months from the date this Agreement is entered into force, a bank guarantee on first demand or some other appropriate means of securing the payments acceptable to both Contracting Parties in the amount of at least one average monthly supply from the preceding year. The instrument guaranteeing the payment shall be continuing and convertible.

30.3. Should a Shareholder fail to meet its obligation under the preceding Paragraph, at the expiration of a subsequent 8-day payment period, the Company may terminate any further supplies and sell the energy on the market. If the income realized by the Company as a result of the sale of such energy on the market proves insufficient to cover all expenses, the Shareholder shall remain liable to the Company for payment of that difference. The Company shall reestablish the supply to the Shareholder upon payment of all outstanding obligations.

NE Krško operating risks

Article 31

31.1. If the nuclear power plant is not operating due to causes which cannot be attributed to any of the Shareholders, and which cause is outside of the actual plant and could not have been foreseen, and its consequences could not have been avoided or remedied (Force Majeure), or due to a cause which could not have been foreseen, and the consequences could not have been avoided or remedied (event), both Shareholders shall jointly cover the expenses incurred, in equal proportions.

31.2. The actions of state authorities or local self-governing authorities, except the actions related to nuclear safety, shall not be construed as Force Majeure.

31.3. If the circumstances from Paragraph 1 of this Article should continue for the term exceeding 12 (twelve) months, and the Shareholders do not agree otherwise, the procedure of premature shutting down of NE Krško shall be performed.

Company bodies

Article 32

The Company bodies are:

- THE MANAGEMENT BOARD;
- THE SUPERVISORY BOARD;
- THE SHAREHOLDERS' ASSEMBLY.

The Management Board

Article 33

33.1. The Management Board is comprised of 2 (two) members appointed at the Shareholders' Assembly. The chairman of the Management Board is recommended by ELES GEN d.o.o., while Hrvatska elektroprivreda d.d. Zagreb recommends a member of the Management Board.

33.2. In addition to the general legal requirements, the appointed persons must have five years of professional experience; a university degree (Bachelor's degree) in either technical, economic or legal profession at a minimum; active knowledge of English; organizational skills and managerial abilities.

33.3. The term of the appointment of the chairman of the Management Board and the member of the Management Board is five (5) years, with the possibility of reappointment.

33.4. Should any member of the Management Board, the chairman included, cease its term for any reason whatsoever, the Shareholder who recommended that member is entitled to directly appoint a new member of the Management Board, who will have equal rights and obligations as his predecessor. Promptly upon the appointment, the Shareholder shall convene a Shareholders' Assembly meeting, where the appointment must be decided. The term of the appointment of a Management Board member appointed in such a manner shall continue until the moment the Shareholders' Assembly makes a decision on the appointment in accordance with this Memorandum of Association. Should the Shareholders' Assembly fail to decide on the appointment for whatever reasons, the term of appointment of the directly appointed Management Board member shall continue until the arbitral award under Article 58 hereof.

33.5. Immediately after the appointment of the Management Board in accordance with this Memorandum of Association, such board shall, according to the parity principle, appoint no less than four (4) and no more than six (6) employees with special authorizations, who shall assume executive directorships.

33.6. The Management Board shall adopt the rules of procedure concerning the activities of the Management Board, which will provide a more detailed mode of operation of the Management Board.

Representation

Article 34

34.1. The Company shall be represented independently by the chairman and the member of the Management Board, within the limits specified herein.

34.2. The Shareholders' Assembly may specify to the Management Board and other persons authorized to represent the Management Board special internal limits to the right of representation, which limits shall not be entered into the court register. The Management Board and/or some other person authorized to represent must adhere to such specified limits.

Business Management

Article 35

35.1. The Management Board shall manage the Company business.

35.2. Decisions by the Management Board within the scope of the management of Company business shall be made by consensus of all board members, except as set forth in Paragraph 3 of this Article. If no consensus is reached as to a decision, such decision shall be submitted for consideration and decision-making to the Company Supervisory Board, in accordance with the provisions of this Memorandum of Association and the Rules of Procedure concerning the activities of the Management Board.

35.3. To prevent possible obstruction in decision-making, when a consensus cannot be reached within a parity composed Management Board, the vote of the chairman of the Management Board will be the deciding vote (the casting vote). The casting vote of the chairman of the Management Board is used only in exceptional circumstances, and only when failure to reach consensus in the Management Board might:

1. jeopardize the safety of the plant operation,
2. cause substantial risk to the accomplishment of the goals determined by the adopted annual plan,

3. cause significant damages to the Company.

35.3.1. If the chairman of the board has used the casting vote, he must immediately request the chairman of the Supervisory Board to convene a meeting of the Supervisory Board during which the use of casting vote will be reviewed and appropriate measures decided.

35.3.2. If the casting vote is used, the members of the board who cast their votes against the decision shall not be held liable for any damage that might arise from such decision of the chairman of the board.

35.4. Within the scope of the management of Company business, in conformity with the law and this Memorandum of Association, the Management Board is particularly required to do the following:

1. define the Company business policy,
2. independently enter into legal transactions and manage day-to-day operations,
3. enter into agreements with employees,
4. maintain business records and prepare and disclose financial reports,
5. furnish the Supervisory Board with business reports each quarter,
6. determine the internal structure of the Company and adopt any other acts,
7. implement the decisions adopted by the Shareholders' Assembly and/or the Supervisory Board,
8. prepare decisions to be made by the Supervisory Board, for the purpose of granting approval,
9. inform other Company bodies, and make appropriate decision within that scope,
10. adopt general resolutions, unless pursuant to this Memorandum of Association or law that is explicitly within the scope of another Company body,
11. enter into and sign collective agreements with unions,
12. care for the development of safety culture in the Company and for implementation of high operational standards,
13. take measures for the purpose of nuclear safety and its implementation, and observe all elements required for safe and stable operation of the nuclear power plant,
14. provide measures required for protection of the employees and population from the source of ionizing radiation in the event of a nuclear accident,
15. govern obligations in conformity with law and regulations that define the dismantling of the nuclear power plant,

16. execute the obligations set forth by the relevant provisions of the Bilateral Agreement,

17. transact any other business set forth by law and this Memorandum of Association.

35.5. The rights and obligations of the chairman and the member of the board shall be defined by an agreement to be entered into with the Management Board by the chairman of the Supervisory Board on behalf of the Company.

Supervisory Board

Article 36

36.1. The Company Supervisory Board is comprised of six (6) members.

36.2. In principle, the Supervisory Board members are selected from the ranks of experts in the fields significant for the Company's operations.

36.3. As an exception to the parity principle, representatives of the employees of NEK d.o.o. (wider organization) are entitled to participate in the meetings and decisions of the Supervisory Board, but only when legal employment issues concerning the employees of NEK d.o.o. are being discussed and decided upon. In such cases, the Supervisory Board consists nine (9) members in three parts, with an equal number of Slovenian Shareholder representatives, Croatian Shareholder representatives and NEK d.o.o. employee representatives.

Article 37

37.1. Members of the Supervisory Board shall be appointed by the Shareholders' Assembly based on recommendations by the Shareholders in such a way that each respective Shareholder recommends three (3) members of the Supervisory Board. The representatives of the employees are appointed by the Shareholders' Assembly in accordance with the regulations relating to employees' participation in management.

37.2. Any such recommendation shall be accompanied by a written statement with which the person recommended as a member of the Supervisory Board, and who is assuming such position for the first time, declares readiness to perform the duties of a member of the Company Supervisory Board and confirm there are no legal impediments to the performance of such duty.

37.3. In addition to the general legal requirements, the selected persons must have five years of professional experience and at least a university education (Bachelor's degree). This requirement does not apply to employee representatives who take part in the work of the Supervisory Board.

Article 38

The term of the appointment of the Supervisory Board members shall be four (4) years, with possible reappointment.

Article 39

39.1. The Supervisory Board appointed at the Shareholders' Assembly meeting must be formed within 8 (eight) days from the date of appointment. At the forming session of the Supervisory Board appointed at the Shareholders' Assembly meeting, the members of the Supervisory Board shall elect the chairman of the Supervisory Board and his deputy.

39.2. The chairman of the Supervisory Board shall be appointed from among the members recommended by the representative of the Shareholder from Croatia, while the deputy shall be appointed from among the members recommended by the representative of the Shareholder from Slovenia.

Article 40

The Supervisory Board performs particularly the following activities:

1. supervises the management of Company business,
2. convenes the Shareholders' Assembly as needed,
3. furnishes the Shareholders' Assembly with written reports on the performed supervision,
4. consents to annual budget and long-term investment plans,
5. gives prior consent to decisions made by the Company Management Board on the investments into the Company, and on the assumption of liabilities on behalf of the Company in excess of USD 2,000,000.00 (two million US dollars), except in cases of alienation or the acquisition of real property, which shall be decided upon by the Shareholders' Assembly,
6. gives opinions on annual reports,
7. represents the Company in relation to the members of the Management Board,
8. consents to decisions made by the Management Board if required by a special act or by this Memorandum of Association,
9. acts as a second-instance body in relation to any matter that requires second-instance procedures and where the Management Board acts as the first-instance entity,
10. adopts the rules of procedure concerning its own activities,
11. appoints and relieves members of its commissions for the purpose of preparing the decisions it makes and the supervision of their implementation,

12. makes decisions in cases when the Company Management Board cannot make its decision due to lack of consent,
13. following recommendations by the Management Board, appoints and relieves members of the independent committee for security analysis (hereinafter: ISEG),
14. reviews reports made by ISEG,
15. implements obligations set forth by relevant provisions of the Bilateral Agreement,
16. performs other activities it is expressly charged with pursuant to the Bilateral Agreement, law, and this Memorandum of Association.

Article 41

41.1. Each member of the Supervisory Board has one (1) vote.

41.2. The Supervisory Board decisions are valid if the majority of member votes is represented at a given session. A decision is valid if it is adopted by a majority of votes of all members of the Supervisory Board. These provisions shall be applied accordingly also when the Supervisory Board is acting as set forth in Article 36 Paragraph 3 of this Agreement.

41.3. If none of the Supervisory Board members require a holding of a session, the Supervisory Board may make decisions without holding sessions through consultations with the members. Such decisions must be verified at the first following Supervisory Board session.

Article 42

The Supervisory Board shall adopt its Rules of Procedure with detailed regulations of the Supervisory Board activities. The Supervisory Board must adopt the Rules of Procedure at the first session following the constitutive session.

Article 43

The Supervisory Board members shall be entitled to compensation for their work on the Supervisory Board in accordance with a Shareholders' Assembly resolution.

Shareholders' Assembly

Article 44

44.1. The Shareholders' Assembly meets at least once a year (regular Shareholders' Assembly).

44.2. Decisions of the Shareholders' Assembly shall be made at Shareholders' Assembly meeting with the consent of both Shareholders unless is otherwise stated in this Agreement for a particular case. The Shareholders' Assembly meeting is not necessary if the Shareholders consent in writing to the decisions that have to be made.

Article 45

45.1. Regular Shareholders' Assembly meetings must be held every year within one month of the preparation of annual report for the previous business year. Shareholders' Assembly meeting may be convened as necessary, particularly when relevant decisions of significance for the Company have to be made, in other words when the interests of the Company thus require.

45.2. Shareholders' Assembly meetings shall be convened by the Management Board by registered letter dispatched to the Shareholders, designating the venue, time and agenda. The Shareholders shall receive the invitation at least seven days prior to the Shareholders' Assembly meeting, with the agenda to be discussed duly attached, as well as appropriate documents relating to the agenda, if necessary.

45.3. The invitation to a Shareholders' Assembly meeting under the preceding Paragraph shall also include an alternate date, venue and time for a Shareholders' Assembly meeting to be held in case the Shareholders' Assembly meeting fails to take place because of absence of one of the Shareholders. The decisions made at the subsequent Shareholders' Assembly meeting shall be valid without regard to whether both Shareholders are present at the meeting or only one. The subsequent meeting shall be held at least five (5) days after the originally convened meeting.

Article 46

46.1. Any Shareholder may request that the Management Board convene a Shareholders' Assembly meeting at any time. If the Management Board fails to do so within fourteen (14) days from the date of receipt of such request, that Shareholder may convene a Shareholders' Assembly meeting directly, in the manner set forth in the preceding Article of this Agreement.

46.2. The invitation shall be delivered at least fourteen (14) days prior to the date of the Shareholders' Assembly meeting, exclusive of the day of the mailing and the Shareholders' Assembly meeting day. The mailing address for the invitation shall be the last known headquarters of a Shareholder.

46.3. Shareholders' Assembly meetings shall be held at the Company headquarters if possible. With the consent of all Shareholders, the formalities of convening and holding the Shareholders' Assembly meetings need not be observed, and a decision may be made without a meeting taking place. For this purpose, the consent of both Shareholders must be in writing.

Article 47

47.1. Members shall take part at the Shareholders' Assembly meeting through their legal representatives and/or authorized agents listed in the court register, or through their proxies. The proxy must be in writing, and a proxy must present the original proxy prior to the Shareholders' Assembly meeting.

47.2. In addition to the Shareholders, their advisers may also attend the Shareholders' Assembly meetings.

Article 48

Each Shareholder shall have one vote at the Shareholders' Assembly.

Article 49

49.1. Shareholders' Assembly decides all issues relating to the Company business and management, and particularly:

1. decides on any modification of the Memorandum of Association,
2. decides on the dissolution of the Company and premature winding-up of the plant,
3. decides on any legal status changes of the Company and modifications of the Company structure,
4. adopts general acts of the Company, the adoption of which is the responsibility of the Shareholders' Assembly according to the binding regulations and provisions of this Memorandum of Association,
5. appoints and relieves members of the Company Management Board and members of the Supervisory Board,
6. appoints and revokes authorized agents,
7. decides upon annual balance sheets, profit sharing, and the manner of covering Company losses,
8. decides upon modifications to the Company business, name or headquarters,
9. decides upon consents to respective Shareholders with regard to encumbrance (attachment) of their business shares in the Company,
10. gives consent to the Company Management Board and the authorized agents for alienation and encumbrance of the Company real property,
11. within the scope of its activities, meets the obligations set forth by relevant provisions of the Bilateral Agreement, and
12. performs any other activities that are not within the scope of some other Company body.

49.2. The Shareholders' Assembly shall appoint the recommended members of the Management Board and of the Supervisory Board, if they were recommended in accordance with this Memorandum of Association.

49.3. The Shareholders' Assembly may adopt a resolution regarding the dissolution of the Company only under the conditions set forth in Article 2 Paragraph 5 of the Bilateral Agreement.

49.4. Shareholders' Assembly meetings must be documented in the minutes of the meetings, which must be signed by the member of the Management Board who was present at the relevant Shareholders' Assembly meeting and by the Shareholders.

Employment

Article 50

50.1. The Management Board is obligated to apply the parity principle when selecting employees with special authorizations defined in the Memorandum of Association.

50.2. The Management Board is obligated to determine the job positions for which, taking into account the principles of safety and optimal operation of the nuclear power plant, appropriate representation of professionals from the Republic of Slovenia and the Republic of Croatia will be secured. Any vacancy notices shall be posted by the Management Board in daily newspapers in the Republic of Slovenia and the Republic of Croatia.

50.3. In education, scholarships and professional training, the Management Board shall be governed by the principle of equal rights, regardless of the nationality of the candidates.

50.4. The provisions of this Article shall also apply to current employees.

Business records and annual report

Article 51

51.1. The Company shall maintain business records and prepare annual reports in accordance with the applicable regulations in force in the Republic of Slovenia, unless stated otherwise in the Bilateral Agreement, provided that the Company Management Board shall be liable for the regularity, accuracy, truthfulness and promptness of such records and reports.

51.2. The Company Management Board shall recommend an annual report for confirmation to the Shareholders' Assembly within the period in which the Company is obliged to furnish the relevant bodies and/or third party organizations with such annual reports in accordance with the applicable regulations in force in the Republic of Slovenia.

Allocation of profits and payment of losses

Article 52

52.1. The Company operates on the principle of covering of all expenses, and in principle its operation results neither in losses nor in profits.

52.2. Any possible profits of the Company arising as a consequence of the difference between the actual and the projected income and expenditures, or as a consequence of subsequent tax or accounting modifications, are allocated into the reserves.

52.3. Any possible loss, incurred as a consequence of the difference between the actual and the projected income and expenditures, or as a consequence of subsequent tax or accounting modifications, are paid from the Company reserves.

Company resolutions

Article 53

53.1. The Company, i.e. its bodies, shall pass relevant resolutions of the Company within their scope of activity, when prescribed by the laws of the Republic of Slovenia or required for the Company activities.

53.2. The Company resolutions are the regulations that the Company is required to pass in accordance with the applicable laws of the Republic of Slovenia, as well as the rules of procedure and statutes regulating the internal structure that is significant for the operation and business of the Company, accounting and financial performance, labor relations, disciplinary and material liability of the employees, trade secrets, rights and regulations of the Shareholders and other important matters that the Shareholders' Assembly or some other relevant Company body shall decide upon.

53.3. Until the adoption of the relevant resolutions, all other resolutions effective in the nuclear power plant as of the date of entry into force of this Memorandum of Association shall apply, provided that they are not in conflict with this Memorandum of Association and the Bilateral Agreement.

Trade Secrets

Article 54

54.1. Trade secrets are all of the information defined as such by law, other regulations and the general resolution on protection of trade secrets to be adopted by the Shareholders' Assembly, which represent a secret related to production, results of research or construction work, and any other information which, if disclosed to unauthorized persons, might adversely affect the economic interests of the Company.

54.2. The Shareholders' Assembly undertakes to adopt the general resolution described in the preceding paragraph of this Article immediately after the Company has been

entered into the court register. Promptly after its adoption, the members of the Company bodies, as well as other persons who are obliged to protect trade secrets must become familiarized with the contents of the general resolution.

54.3. Notwithstanding the contents of the general resolution, trade secrets also include such information which, if disclosed to an unauthorized person, would clearly cause significant damage to the Company. The Shareholders, members of the Company bodies, employees, and other persons, shall be liable for disclosure of trade secrets if they were aware or had to be aware of the significance of the information in question.

54.4. No information that is public according to law or information concerning violations of law or of good business practice shall be declared as a trade secret.

Article 55

55.1. The Shareholders' Assembly shall establish the manner of protection of trade secrets and the liability of persons required to protect them by means of a general resolution mentioned in the preceding paragraph.

55.2. Third persons are also required to protect trade secrets, provided that they were aware that such information was considered a trade secret.

55.3. Any actions contrary to the law and the will of the Company, through which third persons would attempt to acquire trade secrets of the Company are prohibited.

Expenses

Article 56

Any expenses incurred as a result of the execution of this Memorandum of Association, that is, expenses relating to the Memorandum of Association during the process of restructuring and creating the Company, shall be covered by the Company.

Dispute resolution

Article 57

57.1. All disputes arising from or in connection with this Memorandum of Association, i.e. regarding the breach of its provisions, and regarding the termination and rescinding of the Memorandum of Association shall be finally resolved under the Rules of Arbitration and Conciliation (Vienna Rules) at the International Arbitral Center of the Federal Economic Chamber in Vienna, with 3 (three) arbitrators appointed in accordance with said Rules.

57.2. The language of the arbitration is English.

57.3. The said arbitration is authorized to rule equitably, i.e. *ex aequo et bono.*

57.4. The award rendered by the arbitration tribunal as to any specific dispute shall be valid and enforceable for the Shareholders.

57.5. This arbitration is not authorized to settle disputes arising from an inability to make decisions and resolutions on the part of the Company management bodies.

Article 58

58.1. If the Shareholders' Assembly, in other words, the Company Supervisory Board are unable to adopt a resolution due to lack of consent, at the request of one of the Shareholders, the final decision as to the matter in question may be made in a separate proceeding for each respective case by an ad hoc Business Arbitration, which shall be appointed by the Shareholders pursuant to this Memorandum of Association.

58.2. The Arbitration tribunal shall have 3 (three) members (arbitrators). Each Shareholder is obligated to, within 8 days after receipt of request for arbitral proceedings, appoint 1 (one) arbitrator to the Arbitration tribunal and inform the same arbitrator and the other Shareholder in writing thereof. The Arbitration tribunal arbitrators so appointed shall be appointed from a list of arbitrators – twelve (12) neutral experts that shall be appointed by the Shareholders' Assembly at its first meeting, based on Shareholders' recommendations. Each Shareholder shall recommend six (6) arbitrators to the Shareholders' Assembly.

58.3. The appointed arbitrators are obligated to appoint the presiding arbitrator within 5 days from the date of expiration of the period under Article 58 Paragraph 2 hereof. The presiding arbitrator need not necessarily be an arbitrator named in the list. If the arbitrators fail to appoint the presiding arbitrator, the Shareholders shall appoint new arbitrators within 8 days from the expiration of the period set for the presiding arbitrator appointment. If the newly-appointed arbitrators also fail to nominate the presiding arbitrator, such presiding arbitrator shall then be appointed, at the request of any Shareholder, by the chairman of the International Arbitral Centre of the Federal Economic Chamber in Vienna.

58.4. The arbitrators appointed once by the Shareholders for an individual case may, without limitation, be appointed for other cases.

58.5. The seat of the so appointed ad hoc Arbitration tribunal shall be in the Company. All administrative tasks of the arbitration shall be performed by the Company.

58.6. For all other issues, during the proceeding before the Arbitration tribunal the Rules of the Permanent Arbitration under the Chamber of Commerce of Slovenia shall apply accordingly.

58.7. The Arbitration tribunal is authorized to rule equitably, i.e. *ex aequo et bono.*

58.8. The award rendered by the Arbitration tribunal as to any specific dispute shall be valid and enforceable for the Shareholders and the Company.

58.9. Both Slovenian and Croatian languages will be used as languages for the arbitration. The arbitral award will be communicated in Slovenian and translated into Croatian.

Exercise of rights and obligations, and interpretation

Article 59

59.1. The Shareholders particularly undertake to exercise all of their rights and obligations under this Memorandum of Association in the manner that will ensure the highest possible degree of safety of the nuclear power plant operation.

59.2. In interpreting this Memorandum of Association and the settlement of disputes, the equality of rights of the Shareholders shall be observed, unless otherwise specified herein, together with achievement of safe and stable operation of the nuclear power plant.

Amendments of Memorandum of Association

Article 60

Amendments of the Memorandum of Association shall be decided upon by agreement of the Shareholders at the Shareholders' Assembly, and shall be carried out in conformity with the provisions of the CCA.

Severability

Article 61

In the event any one or more of the provisions of this Memorandum of Association shall for any reason be held to be invalid or unenforceable, the remaining provisions of this Memorandum of Association shall be unaffected. In such an event, the Shareholders are obligated to remedy the invalidity or the unenforceability of a provision in a valid manner closest to their economic purpose.

Official language of the Company

Article 62

62.1. The mode and languages of communication among the Company bodies shall be defined by the relevant rules of procedure of such bodies.

62.2. Any business correspondence officially addressed to the Shareholder from the Republic of Croatia shall be sent to the Croatian Shareholder in Slovenian and in Croatian.

Copies of Memorandum of Association

Article 63

This Memorandum of Association is made in six (6) copies in Croatian and in Slovenian, which are equal languages of the Memorandum of Association, of which each Contracting Party will keep two (2) copies in each language, and the remaining four (4) copies will be used for Company registration and other official purposes.

Entry into force

Article 64

64.1. This Memorandum of Association enters into force on January 1, 2002, provided that the Bilateral Agreement is previously entered into force.

64.2. The Management Board and other bodies of NEK d.o.o. shall continue its functions until new bodies are appointed. The Management Board of NEK d.o.o. must convene the Shareholders' Assembly within 3 days from the date of entry into force hereof, in accordance with the provisions of this Memorandum of Association.

64.3. After the Shareholders' Assembly is held pursuant to the preceding Paragraph of this Article, the newly-appointed Management Board shall submit to the court register a proposal for registration of all changes that occurred in accordance with this Memorandum of Association.

******

The Shareholders

HEP d.d. ELES GEN d.o.o.

EXHIBIT 2

PROCEDURE FOR THE EXERCISE OF RIGHT OF FIRST REFUSAL

I.

Unless during the process of liquidation of the Company the Shareholders agree otherwise, the Contracting Parties agree that the real property of the Company shall be sold by international public tender, in the manner stipulated in the following Paragraphs of this Exhibit. The terms of the tender are determined by the liquidator of the Company, with the approval of the Shareholders.

II.

The real property of the Company shall be sold to the highest bidder during the tender mentioned in Paragraph I. The highest bidder means a domestic or foreign legal or natural person who offers the highest price.

III.

The Company liquidator shall, within 30 days from the closing date of the international public tender, deliver to the Shareholders and to the Government of the Republic of Slovenia, in writing and by registered mail, detailed information about the highest bid received for the tender. Such notice shall contain specific information about the real property being sold, the terms of the sale, the time of sale, and other relevant information.

IV.

The Republic of Slovenia has the right of first refusal, provided it offers at least the same purchase price and the same terms of payment as the highest bidder.

If within 60 days from the receipt of notice from Paragraph III of this Exhibit, the Republic of Slovenia fails to deliver to the Company liquidator and the Shareholders a written notice, sent by registered mail, that it is willing to exercise its right of first refusal and to buy the real property under the same or more favorable terms than those offered by the highest bidder, it shall be considered that it did not accept the offer.

If the Republic of Slovenia accepts the offer to purchase the real property, it shall without delay, and not later than 30 days from the date of mailing of the notice of its intention to exercise the right of first refusal, execute the contract for the sale of the real property. If the Republic of Slovenia fails to act in compliance with the provisions of this Paragraph in exercising its right of first refusal, its right of first refusal is terminated.

V.

Transfer of the Company's real property during liquidation proceedings that is not in compliance with the provisions of the previous Paragraphs shall be deemed null and void.

EXHIBIT 3

PRINCIPLES OF THE STRUCTURING OF THE FINANCIAL RELATIONS

(1) ELES GEN d.o.o. shall assume all obligations of NEK d.o.o towards the bank which have occurred as a result of the transfer to NEK d.o.o of the repayment of investment loans made by the Slovene founders, according to the balance on December 31, 2001. Obligations resulting from loans issued to carry out NEK's modernization project will be NEK d.o.o.'s only remaining long-term financial obligations. Until June 30, 2002, the cost of these loans will be borne through the cost of electricity by the Shareholder from the Republic of Slovenia and from that day forward by both Shareholders.

(2) By virtue of the entry into force of this Agreement:

- HEP d.d. waives all claims against NEK d.o.o and ELES d.o.o for damages, i.e. for compensation for undelivered electricity, i.e. for compensation for use of the capital, and in this regard will fully waive all claims in court arising therefrom;
- NEK d.o.o waives all claims against HEP d.d. in connection with delivered power and electricity, and in this regard will fully waive all claims in court arising therefrom;
- NEK d.o.o waives its claims against ELES d.o.o in the same amount as in the previous bullet of this Paragraph;
- NEK d.o.o waives all claims against HEP d.d. in connection with charged fees for financing of the dismantling of Nuclear Power Plant Krško and disposal of radioactive waste from Nuclear Power Plant Krško, and in this regard will fully waive any claims in court arising therefrom;
- NEK d.o.o. waives all claims in connection with pooled resources of depreciation of both founders and claims in connection with the coverage of losses from previous years.

(3) Based on the provisions listed above, NEK d.o.o will rearrange its balance sheet on December 31, 2001 so that:

- it shows neither any claims toward HEP d.d. and ELES d.o.o nor any obligations toward the fund for financing of the dismantling of the Nuclear Power Plant Krško and the disposal of radioactive waste from the Nuclear Power Plant Krško;
- it does not show any obligations toward the bank which occurred as a result of the transfer of repayment of Slovene founders' investment loans to NEK d.o.o. described in Paragraph 1 of this Exhibit;
- based on the conversion of HEP's long term investments and the exemption of the loan, NEK d.o.o's capital will be increased, which capital will, after the payment of the possible uncovered losses, be distributed to the Shareholders in two equal parts, so that the initial capital of NEK d.o.o. reaches the amount listed in Article 2 of this Agreement, and so that any possible remainder is distributed into the reserves;

- any other necessary accounting corrections or changes arising from this Exhibit are executed.

(4) Any possible profit to NEK d.o.o. arising from accounting corrections or changes described in Paragraph 3 of this Exhibit will be tax-exempt.

(5) ELES GEN d.o.o assumes the financial results of all power and electricity produced during the period from July 31, 1998 until the date HEP d.d. begins to take over the electricity again, but no later than June 30, 2002. All the while, NEK d.o.o.'s financial position must not worsen compared to its financial position on July 30, 1998.

(6) The Contracting Parties will ensure that the Shareholders determine, by no later than the end of 2002, whether the company needs additional long-term sources of financing its operating costs, which sources of financing will be secured by a capital increase in NEK d.o.o. or any other appropriate manner.

EXHIBIT 4

BILATERAL COMMITTEE RULES OF PROCEDURE

Article 1

Pursuant to paragraph 1 of Article 18 of the Agreement between the Government of the Republic of Croatia and the Government of the Republic of Slovenia on regulation of status and other legal relations regarding the investment, use and dismantling of Nuclear Power Plant Krško (hereinafter: the Agreement), a Bilateral Committee for Supervision of the Performance of the Agreement and Other Tasks is created in accordance with the Agreement (hereinafter: the Bilateral Committee).

The Bilateral Committee shall consist of the delegation of the Republic of Croatia and the delegation of the Republic of Slovenia. Each delegation has a chairman and four members. As required, each delegation may also include experts.

The chairman of each delegation has a deputy, who is appointed by the members of the delegation.

The Contracting Parties shall inform each other by diplomatic means of the structure of the delegation and any changes thereto.

Article 2

Bilateral Committee shall perform the following tasks:

a) monitor the implementation of the Agreement;

b) confirm the Program of disposal of RW and SNF and approve other related activities;

c) confirm the Program of dismantling of NE Krško and approve other related activities;

d) discuss open issues concerning the mutual relations regarding the Agreement.

Article 3

The Bilateral Committee shall meet at least once a year at alternating the location of the meeting between the territories of both Contracting Parties. As necessary, the chairmen of both delegations may convene an emergency meeting with one consent.

The meeting agenda with related documentation shall be delivered to the members 14 days prior to the meeting.

Upon proposal of either of the Contracting Parties, the meeting will be convened and managed by the Contracting Party who is hosting the meeting.

The host of the meeting shall chair the meeting, and also shall provide all necessary administrative support for the meeting.

Article 4

Any decisions made at the meetings have to be adopted with the consent of both delegations. If a consent cannot be reached, the views of both parties shall be entered into the minutes of the meetings, and the Governments of the Contracting Parties will be notified of such occurrence.

Minutes of the meetings shall be kept and will be signed by both chairmen of the delegations at the end of the meetings.

Article 5

The official languages of the Bilateral Committee are Croatian and Slovenian.

Article 6

Each Contracting Party shall bear the costs incurred by its delegation. The host of the meeting shall bear the costs of conducting the meeting, and other costs arising from the work of the Bilateral Committee shall be borne by both Contracting Parties in equal proportions, unless agreed to otherwise.

INDIVIDUAL OPINION OF JAN PAULSSON

(pursuant to Article 48(4), ICSID Convention)

1. Incidental divergences with fellow arbitrators do not, in my view, necessarily require written expression. I have never before felt impelled to dissent. In this instance, I unfortunately find myself in disagreement with respect to the decisive proposition advanced by my two esteemed colleagues, which as far as I can see could be obtained only by an impermissible rewriting of the Treaty we are bound to apply. Given my duty to exercise independent judgment, I find it impossible to subscribe to the decision, and necessary to record my reasons for differing. My Individual Opinion is lengthy, because it seems fair that I should not content myself with criticising what I view as the majority's decisive error (this can be done, as will be seen, in a few paragraphs). I thus also (i) set out what I view as the proper solution and (ii) expose a number of *fausses pistes*.

2. HEP, a Croatian Government-owned joint stock company, has brought this arbitration against Slovenia under an agreement signed by Ministers representing Slovenia and Croatia on 19 December 2001. HEP properly refers to this instrument as a treaty, and indeed invokes the Vienna Convention on the Law of Treaties ("the VCLT") as applicable to its interpretation. It therefore seems appropriate to refer to it as "the Treaty." HEP claims damages on account of non-delivery of electricity as from 1 July 2002 to 19 April 2003. And yet:

(i) HEP is not a signatory of the Treaty;

(ii) the Government of Slovenia does not produce or market electricity; and

(iii) above all, the Treaty simply does not contain an undertaking to deliver electricity as from 1 July 2002.

3. The first two problems would perhaps not have sufficed to cause me to part ways with the majority; with some legal footwork they could have been sidestepped. (Whether the majority have indeed succeeded in finding a solid path remains, however, a matter of doubt; see Paragraph 75 below.) But to conclude that a treaty which does not

establish an obligation of delivery nevertheless creates liability for non-delivery is one long bridge too far. I find no words in the Treaty that support such an extraordinary outcome.

4. I have naturally sought an overriding cause for this sharp divergence. It appears to me that there are in fact two related causes.

5. The first is a basic difference of approach, in which the majority's natural desire to reach a result that they consider fair and reasonable leads them to imply terms that are not in the Treaty, to ignore terms that *are* in the Treaty, and to give retroactive effect to a Treaty when neither its express terms nor its object require retroactivity. I would have great faith in my colleagues, whom I know well and whose views I often share, if they were entrusted with a mission of determining matters of fairness and reasonableness. Yet this Tribunal has not been authorised to decide the dispute *ex aequo bono* (as would have been required under Article 42(3) of the ICSID Convention). Even if the contrary were true, we would not be in a position to exercise that discretion at this stage of the case. The transformations attendant on the breakup of Yugoslavia gave rise to complex disputes that, as of the signing of the Treaty, had been ongoing for a decade. Originally, nuclear plants had been envisaged to be built in Croatia as well as in Slovenia. The plan for a Croatian plant was abandoned; Croatia became a customer of the plant in Slovenia, but no longer as a fellow federated State within Yugoslavia. This led to predictable divergences. Slovenia invoked international obligations requiring significant investments for Krško NPP ("the Plant"). (This factor is conspicuously absent from the majority's account under the rubric "The Nature of the Dispute", paras. 6-15.) HEP objected that the expenses had been budgeted unilaterally, and were therefore not opposable to it. On the Slovenian side, it was said that HEP's unjustified interruption of off-take threatened the Plant's financial ruin. HEP retorted that the cause for these difficulties was a failure to respect its right of participation in matters of governance. The list goes on, and the complications are endless. I simply do not see how we could at this stage assess the equities of a long narrative where sharply opposed theses have not been fully presented or examined.

6. The second cause of my disagreement is a difference in our understanding of the bargain set out in Exhibit 3 to the Treaty. For the majority, that bargain includes a "critical date" of 30 June 2002. If electricity did not begin to flow to HEP on that date, they apparently believe, it became inequitable to enforce the other terms of the bargain – which, in their view, were all to take effect as of that purportedly "critical date" – without compensating HEP. The problem with this

analysis is not only that it is incorrect in principle to rewrite the Treaty to comport with post hoc notions of equity, but that it is unnecessary to do so. The Treaty does not say that the other elements of Exhibit 3 take effect on 30 June 2002. The perceived unfairness to HEP simply does not arise. Ordinarily, the "critical date" for any treaty requiring ratification is the date when the treaty enters into force, and so it is here. Most notably, until the Treaty entered into force and HEP began receiving and paying for electricity, Croatia (and HEP) had no obligation under the Treaty to bear the Plant's modernisation costs. Also, while Slovenia had taken the view that HEP would have such an obligation if the Treaty had not been concluded, all of NEK's claims against HEP were in any event waived as of the date the Treaty entered into force – including, therefore, any claim for modernisation costs accruing between 30 June 2002 and the Treaty's entry into force. The majority apparently believe that it would be inequitable for HEP not to receive electricity on the same date that it assumed 50% responsibility for modernisation costs and exchanged mutual waivers of claims with NEK. But there is no need to imply terms or to introduce retroactivity to achieve that result: the Treaty's text already provides for all of those elements to take effect on the same date. The fact that that date is the Treaty's entry into force, rather than 30 June 2002, does not change the essence of the Exhibit 3 bargain; nor does it render it less equitable. On a proper reading of the Treaty, HEP starts sharing responsibility for costs as of the day electricity deliveries commence, after the Treaty's entry into force.

7. I moreover feel constrained to express my disappointment upon reading paras. 11-12 of the majority's Decision, which appears in what one would expect to be an objective introductory section of the Decision ("The Nature of the Dispute"). These passages are, in my view, anything but neutral; they read like pleadings on behalf of HEP and seem intended to induce the reader into a strong intuitive sense of the essential fairness of HEP's position, and thus to lay the groundwork for a section of the Decision, commencing with para. 191, entitled "Good Faith". The fact is that these two paragraphs express views of great controversy. Naturally arbitrators have the authority to resolve controversies, but only after examining both sides of the debate and giving reasons for their findings. Here the majority seem to reverse-engineer from their desired outcome, which becomes clear when one reaches para. 191 and its remarkable statement that in treaty interpretation good faith is "the core principle about which all else resolves". This follows the even more curious affirmation in para. 176 that the degree of clarity of a treaty term does not give it "greater or lesser force". I shall revert to this matter in due course (see Paragraphs 23 and 39-51 below).

The merits in a nutshell

8. NEK operates the Plant; its Slovenian and Croatian customers are ELES and HEP, respectively. For HEP's claim to prosper, it must prove that from 1 July 2002 it was to receive (i) electricity from the Plant or (if the Treaty had not entered into force by that time) (ii) the benefit of the price at which electricity would have been delivered between 1 July 2002 and the date of entry into force. (This benefit is, on HEP's view, the difference, if any, between that price and that of the alternative supply HEP was forced to purchase elsewhere.) In short, HEP's claim is that from 1 July 2002 Slovenia had an obligation to supply electricity to HEP, or its monetary equivalent.

9. The problem is that the Treaty does not say so.

10. The majority reason that the settlement of financial issues in Article 17 and Exhibit 3 of the Treaty assumes a general point of equilibrium as at 30 June 2002, irrespective of ratification; and that the general financial settlement with respect to the past somehow overrode (or expanded upon) the explicit terms of the Treaty (see Paragraph 13 below) that deal with the specific future obligation to supply electricity. I fail to see how this is a conceivable construction of the terms of the Treaty.

The key terms of the Treaty

11. The Treaty was ratified by Croatia on 3 July 2002 (i.e. *after* the "equilibrium" date of 30 June assumed by the majority), and by Slovenia (after intense public and parliamentary debate) on 25 February 2003. It entered into force, in accordance with the mechanism defined in Article 22(4), on 10 March 2003, when Slovenia's ratification was received by Croatia. Since then, it has been performed continuously by both sides.

12. The Treaty defines no deadline for its ratification and entering into force.

13. The duty to supply power is dealt with in Article 5(2) of the Treaty as follows:

> *The Contracting Parties [i.e. the two States] agree that the Company [i.e. NEK] shall deliver the produced power and electricity to the Shareholders in equal proportions, half to each Shareholder, until the end of the regular useful life of the nuclear power plant in the year 2023, i.e.* [sic; it appears that "i.e." should be read as "or", T, Day 4, 11:34] *until the extended useful life of the power plant, if approved (hereinafter: useful life).*

Article 5(4) deals with the routing and cost of transmission in very general terms ("shortest transmission routes … transmission costs in accordance with the existing and international practices"). Article 5(6) establishes that the cross-border transmission does not attract customs duties.

14. The Treaty nowhere defines a starting date for the supply of power. The operative date is therefore the date of the Treaty's entry into force. Neither side has suggested otherwise.

15. Article 17 of the Treaty, entitled "Past Financial Issues," reads as follows:

> *(1) Mutual financial relations existing up to the signing of this Agreement between NEK d.o.o., ELES d.o.o., ELES GEN d.o.o. and HEP d.d. shall be regulated in accordance with the principles set forth in Exhibit 3 of this Agreement.*
>
> *(2) The Contracting Parties agree that, as of the date of entry into force hereof, all obligations of NEK d.o.o. to the Fund for financing the dismantling of NE Krško and disposal of radioactive waste from NE Krško, which obligations arose from the application of the Act on Fund for Financing of Dismantling of NE Krško and Disposal of Radioactive Waste from NE Krško ("Official Gazette" of the Republic of Slovenia No. 75/94), shall cease to exist.*

Exhibit 3 is referred to nowhere else in the Treaty but in this Article 17(1).

16. Paragraph (1) of Exhibit 3 deals with responsibility for past loans on the books of NEK. They fall into two categories:

- On the one hand, insofar as they represented original capital loans from Slovenian sources carried in the accounts of NEK as of 31 December 2001, they would be entirely assumed by ELES.

- On the other hand, the reimbursement of loans extended to NEK to finance its modernisation programme would be repaid "through the cost of electricity" (i) entirely by the Slovenian shareholder until 30 June 2002 and (ii) thenceforth by both shareholders. **This is the sole Treaty provision from which HEP infers that Slovenia is liable for the consequences of non-delivery of power by the Plant to HEP commencing on 1 July 2002.**

This arrangement was not explicitly conditioned on the entry into force of the Treaty. There is of course no reason why it should; every element of a treaty is subject to its ratification, with two exceptions only: (a) provisions regarding its entry into force and the like;[1] and (b) agreements regarding the provisional application of certain or all provisions in a treaty (as to which see Paragraph 62 below).

17. It is therefore noteworthy that Paragraph (2) of Exhibit 3 begins with the words

> *By virtue of the entry into force of this Agreement:*

before setting down five subparagraphs. The last four of these subparagraphs relate to waivers by NEK of various claims *against HEP*. The first subparagraph, by contrast, is this:

> *HEP d.d. waives all claims against NEK d.o.o. and ELES d.o.o. for damages, i.e. for compensation for undelivered electricity, i.e. for compensation for use of the capital, and in this regard will fully waive all claims in court therefrom ...*

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[1] See Article 24(4) of the VCLT.

18. Certain treaties provide a deadline for ratifications, typically by setting forth a fixed date for their entry into force.[2] It would be discourteous to the two States here to assume that they were ignorant of such basic techniques in treaty practice. In his opening statement, counsel for HEP stated:

> *Slovenia has said that nobody really thought about what would happen if the Agreement wasn't ratified by June 30th 2002, and on the whole we agree with that, but it was clearly the working assumption and understanding of the parties that it would be ratified by that time ...* (T Day 3, 110:3)

This seems plausible. Yet the State parties certainly did not exclude post-30 June 2002 ratification. Each did in fact ratify after that date. And each has until now conducted itself on the premise that the Treaty is in force and binding as of the date set out in Article 22(4).

19. It is therefore not open to this Tribunal to find that the unratified Treaty would have lapsed if it had not entered into force prior to 30 June 2002; nor that there was an obligation on either Contracting State to ratify the Treaty by 30 June 2002.

The essential flaw of the Decision

20. HEP bears the burden of showing that by allowing the Treaty to enter into force on 10 March 2003, Slovenia accepted liability, as from 1 July 2002, for covering any cost for electricity supplies in excess of the cost of (undelivered) supplies from the Plant. I believe that my colleagues' acceptance of HEP's thesis is unpersuasive for reasons that can be stated in a very few sentences (see Paragraph 23 below).

21. Three crucial paragraphs of the majority's Decision appear as the conclusion of the key section headed "The Treaty's Terms". They read as follows (with emphasis added):

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2 The example given in the UN Handbook on *Final Clauses of Multilateral Treaties* (Sales No. E.04.V.3, 2003), a publication widely available to Foreign Ministries, is Article III(1) of the Agreement Providing for the Provisional Application of the Draft International Customs Conventions on Touring, etc. (Geneva, 16 June 1949), 45 UNTS 149: *ibid.*, at 63.

174. Exhibit 3 is entitled "Principles of the Structuring of Financial Relations". Its paragraph (1) provides that ELES GEN d.o.o. shall be responsible for the repayment of investment loans by the Slovene founders of NEK "according to the balance on December 31, 2001," and that NEK's responsibility for "remaining long-term financial obligations" arising out of "NEK's modernization project" "will be borne through the cost of electricity by the Shareholder from the Republic of Slovenia [until June 30, 2002] and from that day forward by both Shareholders." This ***of course*** *is in line with the* ***parity principle*** *that has governed the two sides since the 1970 Agreement and which* ***permeates*** *the 2001 Agreement (see Paragraphs 196-197, below).* ***Accordingly,*** *HEP's post-30 June 2002 obligation to share NEK's previously incurred modernization costs is part of the financial settlement achieved by Article 17 and Exhibit 3 of the 2001 Agreement. That settlement is a two-way street. Paragraph (5) provides that ELES GEN "assumes the financial results of all power and electricity produced during the period from July 31, 1998 until the date HEP d.d. begins to take over the electricity again, but no later than June 30, 2002."* ***Hence*** *starting 1 July 2002, HEP would share the costs outlined in paragraph (1) in accordance with the new financial terms. As of 1 July 2002, HEP would also be entitled to the financial results of its share of the electricity produced by Krško NPP. While* ***of course*** *NEK could not be compelled actually to deliver electricity to HEP until such time as the 2001 Agreement would enter into force, the terms of the financial settlement concluded, and which* ***perforce*** *took effect with the entry into force of the 2001 Agreement, were based on the financial facts that would flow had HEP been supplied electricity starting 1 July 2002.*

non sequitur

non sequitur

non sequitur

non sequitur

175. Just as Exhibit 3 determines the date as of which the new financial terms would take effect, i.e., the ***"critical date"*** *of 30 June 2002, so, too, does it determine the extent of the waivers contained in Paragraph (2) of Exhibit 3. Paragraph (2) expressly refers to "delivered" and "undelivered" electricity without also giving a date against which electricity is to be classified as "delivered" or "undelivered".*

The same applies to the subsequent waivers in which NEK waives "all claims against HEP" relating to the dismantling of the Krško NPP, disposal of waste, "depreciation" and "coverage of losses from previous years."

176. It is important to note that the above view is reached as a result of construing the words of the 2001 Agreement as prescribed by Articles 31 and 32 of the VCLT. Nothing more and nothing less. While the parties have debated vigorously the issue of whether an obligation can be "implied" in an international agreement, that debate is rendered pointless by the terms of VCLT Articles 31 and 32, which do not categorize treaty provisions as being either "express" or "implied". Hence the VCLT-prescribed interpretive process is just that [sic]. ***No greater or lesser force resides in a term by virtue of the relative magnitude of the clarity with which it has been (or has not been) written.*** *The Tribunal's construction of Article 17 and Exhibit 3 becomes clearer still when, as the VCLT requires, one considers their wording "in light of the [the 2001 Agreement's] object and purpose" and "in their context".*

22. Paragraph 176 is obviously intended to reassure, but saying that one has done "nothing more and nothing less" than construing the words of the Treaty does not make it so. The proposition that "No greater or lesser force resides in a term by virtue of the relative magnitude of the clarity with which it has been (or has not been) written" seems nothing less than revolutionary. (Indeed it is difficult to stifle the impression that this extraordinary declaration betrays an awareness of likely doubts.) It seems not only that the majority, contrary to what they profess, have fastened upon far-reaching *implications*, but that they have moreover built their conclusions on a series of four *non sequitur* sentences, noted in the margin of the quoted text in Paragraph 21. It seems to me that each of them contains assertions which are not justified by any of the analysis. Expressions like "of course" and "perforce" and "permeate" have no weight unless they have some foundation in reason. The same is true of the reference to a "two-way street" as well as of the ceaseless repetition of the expression "parity principle".

23. My reasoning is hardly recondite. The following simple observations with respect to para. 174 of the Decision (quoted in

Paragraph 21 above) are sufficient, in my view, to show the error of the majority's Decision. Relevant passages from Exhibit 3 are of course correctly reproduced just before the four sentences. But the notion that the Exhibit 3 "of course" is "in line" with "the parity principle" that "permeates" the Treaty seems to be an effort to convince by dint of confident expression rather than by reasoning. The essence of this sentence (beginning with the words "This of course") is a mystery. The Decision repeats the expression "parity principle" time and again, as if this uncontroversial element of the case carries some special significance for the issue at hand. The headings throughout the ostensibly objective "Summary of Facts" repeat references to "the parity principle" – although it is the post facto construction of HEP, not an expression used in the referenced documents.[3] The expression first appears in para. 9 of the Decision, where it is said blandly that the 50:50 partnership "became known as the 'parity principle'". (One can only wonder: by whom? in what document? how was it imported into the Treaty?) This is apparently intended to provide an ostensibly factual foundation to the reference, in the first sentence of the section on the Treaty's "Object and Purpose" (para. 177 of the Decision), to the proposition that what the States-party were doing was to proceed "in accordance with the parity principle". I have no objection to the expression itself, but rather to its appearance in this portentous manner – as though it were the luminous pathway to a proper disposition of the controversy at hand. It is not. The mantra of "parity" is simply inconclusive as to the issue whether Slovenia in effect promised HEC to cover any adverse financial consequence on account of non-ratification (and therefore non-delivery) as of 1 July 2002. That proposition simply does not flow from the ideas of wiping the *past* "slate clean" and maintaining *future* "parity". The past is the past. The future is whenever the Treaty comes into force. The issue of non-deliveries after signature but before ratification is *in between*. If the States-party had wanted to stipulate some consequences in this hypothesis of the period between signing and entry into force, they needed to do so explicitly. They did not.

- Hence there is no foundation for the four heady leaps of logic that follow. The fact that Farmer Ellis and Farmer Henry agree to settle the accounts of past repairs to the barn made by Ellis cannot possibly, in and of itself, mean that Ellis promises to indemnify Henry if future milk is not delivered. *There is no*

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[3] In para. 191, the majority's Decision asserts that its reliance on its view of good faith "*does no violence*" to the terms of the Treaty. That is hardly good enough. The Tribunal's duty is to decide *in conformity with* the terms.

connection. That would be a separate deal and would have to be explicit.

- To say that the cost of all hay to feed the cow will be covered by Farmer Ellis until 30 June cannot be given the meaning – "*Hence*" – that *Farmer Henry* will share those costs starting on 1 July. We need to know when the two are going to begin sharing the milk. If that date is prior to 1 July, Henry will get something of a free ride. If it is subsequent – *any time* subsequent – he will have to pay his share, then and only then.

- There is no corollary that Henry shares the milk as of 1 July. That remains to be agreed.[4]

- There is no warrant to say that "*of course*" Henry is entitled to the financial benefit of undelivered milk as from 1 July. This seems to be the concrete meaning of the majority's abstract idea of "a financial settlement" which "*perforce*" took effect upon ratification and was "based on the financial facts that would flow" had supplies begun 1 July 2002.[5]

24. And so it seems the majority are walking on thin air when, as they reach para. 175, they refer to the "critical date" of 30 June 2002. One searches in vain for any reference to the words *critical date* in the Treaty or in Exhibit 3. (In contrast, "delivered" and "undelivered", the two other expressions that appear in inverted commas in para. 175, do come from Exhibit 3.) The ostensible quotation of "critical date" appears again in para. 178, which is a part of the discussion of the Treaty's "Object and Purpose" – a rather facile demonstration for the majority once they have achieved the four leaps of para. 174. By now one wonders who actually used these quoted words. The answer comes in paras. 185-186; they were used in the witness statement prepared for this arbitration under the signature of a leader of the Croatian negotiating team, Dr Granic. The expression loses valence as the mere *ipse dixit* of a litigant.

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4 Might one wonder who pays for the hay between 1 July and whenever Henry begins to receive (and pay for) the milk? Well, that would surely be Ellis, unless he wants the cow to starve. Is this a lacuna in the agreement? We do not have to know, because no one is suing Ellis. Anyway, Ellis took all the milk and part of the price he paid for it therefore covered the hay.

5 The concept of "financial facts" is unclear to me, and hardly seems equivalent to an undertaking in the Treaty *to compensate for lost future deliveries in the event of non-ratification* – which could easily have been drafted, but evidently was not agreed.

25. I perceive no logical reason why 30 June 2002 should have been an inherently "critical date" in terms of deliveries. There is no basis upon which to infer from the terms of the Treaty that it would be *inherently disadvantageous* to HEP for deliveries to commence at some time after 30 June 2002. If HEP did not receive the electricity, it would not pay for it – including the built-in surcharges which would up to that date have been paid by the Slovenian side. There is no premise in the Treaty to the effect that the prices ex-Krško were particularly advantageous to HEP, so that alternative purchases would have been costlier. This can only be observed post facto in light of evolving market realities, such as HEP's own downstream commitments, and the cost and availability of alternative sources. If the 30 June 2002 date had been "critical" to Croatia, it could have withheld its ratification – or suspended it pending Slovenia's ratification.

26. If the majority feel that their approach was necessary to avoid a *conceivable* disadvantage to HEP, one can only counter that their rewriting of the Treaty in fact causes a *definite* unjustified prejudice to Slovenia. Consider the following:

(a) Neither Article 17 nor Exhibit 3 create, in terms, a separate financial obligation in case the Treaty (and therefore supply of electricity) have not come into being before 1 July 2002.

(b) It is difficult to see how such an obligation could be simply read into the Treaty, absent express terms to that effect. The obligation would be draconian; it would amount to a promise to pay HEP:

(i) the difference between the price of electricity supplied by the Plant and whatever price of electricity HEP could procure elsewhere,

(ii) without receiving HEP's contribution towards the modernization of the Plant,

(iii) for any length of time from 1 July 2002 to one day before the end of the useful life of the Plant (i.e. more than 20 years), and all this

(iv) whatever the reason for the Treaty's non-entry into force during this time, and whether or not Slovenia had ratified the Treaty before Croatia did.

27. There is nothing left to analyse under Article 17 and Exhibit 3. But it is not the end of the matter. The supposed obligation to pay the monetary value (to HEP) of electricity from a given date (1 July 2002) onwards can be regarded only as a substitute for the obligation to supply actual electricity. This is a matter which, had the parties wished to do so, would have been regulated in Article 5(2). They did not. What they have done, in fact, is to indicate a date as of which the cost of electricity supplied in accordance with Article 5(2) would incorporate a modernization surcharge. That date was 1 July 2002 (Paragraph (1) of Exhibit 3). It is agreed by all that it was assumed that by that date the Treaty would have entered into force. But I cannot share the majority's view that this assumption can retrospectively be transformed into an obligation for *both* States-party to ratify the Treaty by that date – failing which Slovenia, and Slovenia alone, is to be penalised. That is in my view an elementary error, given that the Treaty was subject to ratification for its entry into force, and that there is no rule of general international law requiring States to ratify international treaties. To decide such matters in the Contracting States' place is what the majority now purport to do. I find this plainly impermissible. (Indeed, although they seem not to have considered the point, the majority's logic would compel the conclusion that the true time-limit for ratification was some unknown date sufficiently in advance of 1 July 2002 – perhaps in May, but who knows? – to allow for technical preparations for the flow of electricity into the Croatian grid.)

28. The majority apparently arrive at this result on the basis of an understanding they have formed that the Croatian side was to service loans for NEK's modernisation project starting on 1 July 2002, irrespective of whether any electricity was delivered. They derive that understanding from a provision regarding the price of electricity until 30 June 2002. Given that this understanding is of the essence to the majority's view of the object and purpose of the Treaty and the equities involved in construing its text, it is useful to look at the relevant Treaty provision closely. The key sentence, the last in Paragraph (1) of Exhibit 3, reads:

> *Until June 30, 2002, the cost of these loans will be borne* ***through the cost of electricity*** *by the Shareholder from the Republic of Slovenia and from*

> *that day forward by both Shareholders.* (Emphasis added.)

29. There might have been some merit in the majority's approach if the sharing of the cost of the loans were an unqualified obligation starting on 1 July 2002. But it is not. The cost of the loans is to be serviced "through the cost of electricity" produced by the Plant, pro rata to deliveries actually made to HEP. Plainly the cost-sharing obligation is conditional upon the electricity-supply obligation in Article 5(2). That latter obligation came into effect as of 10 March 2003. To condition the electricity-supply obligation on the indicative date for the cost-sharing obligation strikes me as unorthodox on any view of treaty interpretation, for it puts the cart before the horse.

30. The text of the Treaty itself simply does not mention the date of 30 June 2002. The delivery obligation is stipulated as extant throughout the useful life of the power plant, but with no starting date. Nor does Paragraph (2) of Exhibit 3, which defines the reciprocal waivers between HEP and NEK, mention any date. That leads to the straightforward proposition that entry into force wiped the slate clean of claims between HEP and NEK, as indeed explicitly suggested by the preambular phrase of Paragraph (2) of Exhibit 3: "By virtue of the entry into force ...".

31. I find it impossible to ignore the striking difference between Paragraphs (1) and (2) of Exhibit 3. In Paragraph (1) of Exhibit 3, the 100% attribution to Slovenia of an electricity-price factor to service loans for NEK's modernisation programme was stated to end on 30 June 2002. Thereafter both shareholders would absorb that factor in the price for their share of delivered electricity. This arrangement was not expressly qualified by any reference to entry into force of the Treaty. On the other hand, the series of reciprocal waivers which are the object of Paragraph (2) of Exhibit 3 are so qualified.

32. This difference creates no difficulty, and should not objectively have caused any doubt in the mind of the members of Parliament in either country. What were they to have made of Paragraph (1) of Exhibit 3, where the 30 June 2002 date does appear? The answer is: (i) that its terms become effective, like any other term of the Treaty, upon entry into force and (ii) that in consequence electricity supplied subsequently to the Treaty's entry into force would be priced to both shareholders with a factor representing debt service for modernisation. The sole significance of the date is thus plain to see. I would put it in a nutshell as follows:

> **If ratification and resumption of deliveries to HEP occurred prior to 30 June 2002, that price-component would be payable by the Slovenian purchaser, ELES, but not by HEP even though HEP was receiving power. *This appears to be the only effect of Paragraph (1); it is a negotiated element of the deal.*[6] After that date, HEP's price would begin to include that component as well, but obviously only from the moment of resumption of deliveries (i.e. following entry into force). There is neither ambiguity nor any problem of logic in either hypothesis.**

33. If ratification and entry into force did not occur prior to 30 June 2002, nothing required that deliveries to the Slovenian purchaser subsequent to that date would bear this charge, the forecast date of 30 June 2002 (Paragraphs (1) and (5) of Exhibit 3) notwithstanding. Nor of course would the Croatian shareholder pay anything for deliveries *not made*.[7] That meant that Slovenia, as a party to the Treaty, did not have any obligation to procure any particular pricing regime applicable to ELES with respect to the time period between 1 July 2002 and entry into force. This left NEK and ELES to sort out the issue of pricing; Croatia had no way of insisting that the modernisation surcharge would be paid by ELES during this period, but on the other hand all indications are that the Slovenian Government (not to mention NEK) wanted this to be done. In any event, nothing turns on this; if for whatever reason this circumstance made the Treaty unpalatable to either Parliament, it was open to its Members to withhold ratification. Both Parliaments, of course, elected the opposite course.

34. Thus, while the Treaty does not regulate the incidence of the modernisation surcharge between 1 July 2002 and the Treaty's entry into force, this is not fatal to the Treaty's object and purpose. There is no reason to put in question, let alone supplement, the express terms of Paragraph (1) of Exhibit 3, for there is no rule requiring that a treaty deal with all eventualities.

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[6] Paragraph (1) appears to be a specific carve-out of the more general principle of Paragraph (2)(5). If so, it is an example of the infinite sub-bargains that are routinely made in complex commercial transactions.

[7] HEP has never questioned its obligation in principle to pay the surcharge from the time deliveries commenced pursuant to the Treaty. Not, it seems, did HEP, at the time before entry into force of the Treaty, offer to pay for the surcharge.

35. Nor is there any residual difficulty with respect to Paragraph (2); and the position can be explained in even fewer words. I would put it thus:

> **The reciprocal waiver of claims would occur by virtue of ratification; absent ratification it would not occur at all. No predefined calendar date is involved. The many waivers of para. 2 could not include claims for undelivered electricity, for the simple reason that there was no defined supply obligation under the Treaty prior to its ratification.**

36. The Treaty wiped the slate clean of claims between HEP and NEK that had arisen before the date of entry into force, as indeed explicitly suggested by the preambular phrase of Paragraph (2) of Exhibit 3: "By virtue of the entry into force ...". The majority point out that Paragraph (2) does not set a specific date as of which claims would be waived.[8] That makes it all the more difficult to understand how that paragraph could waive claims arising before – but not after – 30 June 2002, a date the paragraph neither mentions nor incorporates by reference. Even without the preambular phrase, the natural assumption would be, as with any provision of any treaty not specifying a particular date, that Paragraph (2) was effective as of the Treaty's entry into force.

37. That conclusion is significant in two respects. First, the Croatian side (like the Slovenian side) waived all claims arising from the non-delivery of electricity, making it very difficult to see how HEP can now claim compensation calculated on the basis of "financial facts" said to have flown from the non-delivery of electricity between 30 June 2002 and 19 April 2003. Second, the unfairness my colleagues seem to perceive in not compensating HEP for such non-delivery is based on the mistaken assumption that the benefits HEP

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[8] See para. 175: "[T]he 'critical date' of 30 June 2002 [also] determine[s] the extent of the waivers contained in Paragraph (2) of Exhibit 3. Paragraph (2) expressly refers to 'delivered' and 'undelivered' electricity without also giving a date against which electricity is to be classified as 'delivered' or 'undelivered'". I do not understand why one needs a date in order to "classify" electricity as "delivered" or "undelivered". The point is that *claims* arising from the fact that electricity was delivered and either not taken or not paid for, on the one hand, or not delivered in spite of an obligation to do so, on the other, would be waived; nothing in Paragraph (2) suggests that claims existing as of entry into force would *not* be waived if they had arisen after 30 June 2002. The waivers of Paragraph (2) included all claims arising from the delivery or non-delivery of electricity up to the date the Treaty entered into force – notably including any claim from the Slovenian side that HEP should have been buying electricity from NEK prior to the Treaty's entry into force in order to offset HEP's share of NEK's modernisation or other costs.

received pursuant to Exhibit 3 (including the waivers in HEP's favour in Paragraph (2)) were cut off as of 30 June 2002, a problem that does not arise on a straightforward textual construction of Paragraph (2).

38. To conclude, the States-party to the Treaty were seeking to establish a new framework for their cooperation in the nuclear industry. The *critical date* for that framework was the date the Treaty entered into force. As of that date, the parties would start from zero, with no claims against each other, and their national utility companies would receive electricity and bear the costs of the project on a 50/50 basis, the only proviso being that HEP would not have to pay its full share of the costs until 30 June 2002 at the earliest. Nothing in the text of the Treaty, including Exhibit 3, creates an obligation to supply HEP with electricity before the Treaty enters into force or a corollary right for HEP to receive compensation for non-delivery during that period.

Fairness, reasonableness, and extrinsic evidence

39. As I believe the foregoing section makes plain, the text of the Treaty, including Article 5(2) and Exhibit 3, cannot plausibly be read to establish the obligation that the majority now impose on Slovenia. There is no ambiguity that would justify recourse to the secondary interpretive sources mentioned in VCLT Article 32. Yet the majority rely to a great extent on various extrinsic expressions of the Contracting States' intentions. This approach may be motivated, as I have suggested above, by a conviction that it would be unfair, or contrary to the essence of the bargain underlying the Treaty, if HEP were not compensated for the delay in receiving electricity caused by Slovenia's "late" ratification of the Treaty. (As I note in several places below, the majority relies explicitly on what they perceive as tardy ratification by Slovenia. The fallacy of this argument becomes apparent if one considers that the outcome of the majority's reading of the Treaty would be the same even if *Croatia* had ratified second, and after 30 June 2002.) Again, the perceived unfairness is illusory; the majority apparently do not appreciate the significance of the fact that HEP is relieved of any liability to contribute to the costs of the Plant, including modernisation or decommissioning costs, until the date the Treaty enters into force. In any case:

- the result commanded by the Treaty text is neither "manifestly absurd [n]or unreasonable" so as to permit recourse to VCLT Article 32;

- the construction urged by HEP and accepted by my colleagues, on the other hand, *could* lead to substantial unfairness or even absurdity;

- over time, that construction would have created an increasingly powerful disincentive for Slovenia to ratify the Treaty; and

- there are no expressions, by authorised persons at a relevant time, of an intention to compensate the Croatian side for the non-delivery of electricity between 30 June 2002 and the Treaty's effective date.

In my view, there is therefore no need to resort to these sorts of policy considerations, nor to a highly contested inquest into non-textual evidence of what the parties "really" had in mind. But in view of the approach taken in the Decision, some brief observations may be in order, first as to its remarkable view of the law of treaties, and secondly as to its conceptual errors even on the premise that arbitral tribunals may proceed on unrestrained teleological inquiries.

40. I have no concern whatever that my colleagues, any more than I, harbour some a priori preference for either party. My confidence in the majority's impartiality is total. Our difference is purely a matter of principle, but that does not make it less acute. It is my view that the majority have engaged in a remarkable rewriting of history, as though the epic battles that led to the VCLT had gone the other way. To disregard the VCLT's vindication of Gerald Fitzmaurice's view of treaty interpretation is the jurisprudential equivalent of pretending that Octavian lost at Actium. Fitzmaurice wrote in 1957 – citing the ICJ's decision in the *Iranian Oil* case – that treaty "texts must be interpreted as they stand and, *prima facie*, without reference to extraneous factors".[9] He, along with Humphrey Waldock, his successor as Special Rapporteur on treaty law of the International Law Commission, never gave in to the onslaughts of the advocates of "total context". In the end, as Douglas Johnston put it in his learned work, *The Historical Foundations of World Order*: "The victory of the 'textual' approach in the ILC and at the Vienna

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[9] 33 BYIL 203 at 212. Fitzmaurice derived six canons of interpretation from the jurisprudence of the International Court of Justice, three of which were primary and three secondary (subject to the primary ones). The primary canons were those of "textuality", "natural and ordinary meaning", and "integration" of specific terms into the whole of a treaty.

conference was a victory for formalism and for Sir Gerald Fitzmaurice".[10]

41. This historical fact may not be to the liking of those who would favour a more expansive view of the decision-making power of international tribunals, but it cannot be denied. More importantly, it is the bedrock of the international law of treaties, and it is therefore impermissible to ignore it when giving effect to what States understand they do when they sign treaties. It is important to see precisely how the majority, I regret to say, appear to turn the VCLT on its head.

42. The general rule of the VCLT is to the effect (Article 31) that a treaty:

> *shall be interpreted in good faith in accordance with the meaning to be given to the terms of the treaty in their context and in the light of their object and purpose.*

43. The majority appear simply to have erased the words "in accordance with the meaning to be given to the terms of the treaty in their context" and gone on to determine the outcome that commends itself to them. I shall revert to this in a moment.

44. A critical aspect of the words just quoted is the use of the pronoun *their* rather than *its*. The permissible context is *the context of the terms* of the treaty and *not the context of the treaty generally*, in the way desired by the "total context" proponents. This is precisely how the textualist approach carried the day when the VCLT was signed in 1969.[11] Professor Johnston confirms this, *ibid*, noting that Article 31 restricts "context" to the text of the treaty (along with its preamble and annexes), and to two other types of text:

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10 At p. 33 (2008).

11 Waldock, the last Special Rapporteur of the ILC for the VCLT, outlined the following considerations as being of primary importance: "the particular arrangement of the words and sentences, their relation to each other and to other parts of the document, the general nature and subject-matter of the document, the circumstances in which it was drawn up": [1964-II] YBILC at 54. He noted, *ibid.* at 54-55, that he proposed to give effect to Fitzmaurice's "principle of actuality or textuality", contrasting it with "doctrinal differences ... which have tended to weaken the significance of the text as the expression of the will of the parties".

> *(a) any agreement relating to the text which was made between all parties in connection with the conclusion of the treaty,*

and

> *(b) any agreement which was made by one or more parties in connection with the conclusion of the treaty and accepted by the other parties as an instrument related to the treaty.*

As far as I can discern, the majority's Decision proceeds in ignorance of this fundamental and much-discussed constraint on the freedom of international judges and arbitrators to interpret treaties. My observation seems to be confirmed by the very heading of their discussion at paras. 181-182, namely "The Treaty's Context". They seem to ignore that they are allowed to refer only to the context *of the terms* of the Treaty, i.e. the internal consistency of the text as one whole. This fundamental error, it seems, has freed the majority to impose its vision of commercial reasonableness on the entire history of Krško NPP. This is not what States submit themselves to when concluding a Treaty. The majority's vision of commercial logic leads them to all manner of reading between the lines of the Treaty and of various more or less related, more or less contemporaneous, and more or less superseded documents. This is what apparently inspires their constant repetition of the expression "parity principle" (per se unobjectionable) and to their assertion in para. 178 that a "settlement was keyed to the presumed time of entry into force" of the Treaty (as far as I can see a pure invention). There is no sequence of agreed words anywhere that sustains the proposition essential to HEP's claim.

45. In recent years, voices have been heard to the effect that the strongly textual philosophy of the VCLT should be tempered in the context of broad-based "law-making" multilateral treaties intended to create frameworks for cooperation expected to last into the indefinite future. Whatever views one may have in this regard, they are obviously inapposite to the case of a Treaty like this: a highly technical bilateral agreement intended to resolve a specific problem arising from lengthy factual antecedents well known to both States.

46. Two propositions are salient in the majority's section titled "Good Faith". Both are set out in para. 191:

- in treaty interpretation, good faith is "the core principle about which all else revolves";

- "As both parties agree was their desire, a line is drawn as of 30 June 2002 ...".

47. The reasoning of the majority is that the two States intended to establish a "principle of parity", and *it must follow* that it was to be established as of 30 June 2002 (see paras. 174-175) and therefore the 2001 Agreement has to be read in a way that produces this outcome; a different reading would be contrary to good faith. As noted above, a novel legal proposition has been conceived to advance this kind of reading: "No greater or lesser force resides in a term by virtue of the relative magnitude of the clarity which it has been (or has not been) written" (para. 195). The majority says, in effect, that one may postulate an outcome and force-fit it into the actual text. Nuances and omissions in the text are of no moment. In the result, the majority retains from Article 31(1) VCLT only the elements that confirm their subjective gloss (perceptions of good faith and object and purpose), ignoring those which are of an objective nature (textual terms and context). This is precisely the approach described in Paragraph 7 above, with which I simply cannot associate myself. It lies at the heart of my reason for producing this Individual Opinion.

48. On the majority view, instruments are evidently to be read starting from one's perception of their object and purpose and requirements of good faith, and the express terms are secondary. Yet Paul Reuter explained cogently why interpretation must start from the text and not be bolted onto it:

> *If [the parties have reduced their agreement to a written] document, the intention has become a text by means of a very specific operation, going backwards from the text to the initial intention. Drafting methods and rules of interpretation are therefore two aspects of the same problem viewed from two opposite angles: both deal with an intention embodied in a text. ...*
>
> *The primacy of the text, especially in international law, is the cardinal rule for any interpretation.* ***It may be that in other legal systems, where the legislative and judicial processes are fully regulated by the authority of the State and not by***

> ***the free consent of the parties, the courts are deemed competent to make a text say what it does not say or even the opposite of what it says. But such interpretations, which are sometimes described as teleological, are indissociable from the fact that recourse to the courts is mandatory,*** *that the court is obliged to hand down a decisions, and that it is moreover controlled by an effective legislature whose action may if necessary check its bolder undertakings. When an international judge or arbitrator departs from a text, it is because he is satisfied that another text or practice, i.e. another source of law, should prevail.*
>
> *In the interpretation of international law, because of the submission to the* expression *of the parties' intention, it is essential to identify exactly how that intention was expressed and to give precedence to its most immediate manifestation. ...*[12] (Emphasis added.)

49. At the very least, one would have expected the majority to have identified in the object and purpose of the 2001 Agreement the specific reasons for which its reasoning is *compelled* – rather than simply comforted. The closest the majority comes to that is at para. 174, where it is said that the supposed settlement as of 30 June 2002 was "a two-way street". But the text which follows falls short of making good on that assertion. Indeed, the text of fn 152, so far as I can tell, infirms the majority's reasoning. Reference is there made to Articles 10-11 of the 2001 Agreement, which are expressly stated to operate from a given date after entry into force. That fact is said to support the conclusion that "HEP in no way escapes its obligation to contribute its 50 percent share of ultimate decommissioning costs". The opposite appears to be true.

50. Finally, the reverse-engineering of the majority's reasoning becomes apparent at para. 193, where it is said that Slovenia is now, as it were, to atone for the sin of not having "ratified the 2001 Agreement in time for it to enter into force before 1 July 2002". So it is clear that (a) Slovenia was not obligated to supply electricity under Article 5 before the Treaty's entry into force and (b) Slovenia had no obligation under the 2001 Agreement or customary international law to ratify that Agreement on or by a certain date, and yet – to serve an

[12] P. Reuter, *Introduction to the Law of Treaties* (2nd English edn, 1995) paras. 141-143 (emphasis in the original, citations omitted).

obligation imported only by the majority's perception of good faith – it has to take the consequences of not having taken acts which it was not legally required to take.

51. In his voluminous study of *La bonne foi en droit international public* (2000), the Swiss scholar Robert Kolb concludes succinctly at p. 277 that interpretation should not be made to fit a preconceived result, precisely because "good faith forbids it" ("*la bonne foi l'interdit*"). The majority in this case, I fear, have turned this around, following their own intuition that good faith points to a certain result, and that therefore the effort of interpretation should consist of seeking to justify it.

52. Next, some observations of a teleological nature. Even if contrary to my belief ICSID arbitrators had full sway to exercise their imagination in this respect, the circumstances of this case do not lead to the conclusions defended in the Decision. To start with, there is the problematic notion in my colleagues' text that Slovenia accepted an obligation to pay damages for the non-occurrence of an event – entry into force by 30 June 2002 – whose occurrence the majority accepts Slovenia had no duty to procure. This is problematic on both the theoretical and practical planes. One may imagine an understanding that a ratifying party accepts responsibility for *past due performance* of an obligation already in existence, but absent an explicit stipulation to that effect why should a ratifying party assume responsibility for doing something which was never due and which can no longer be done? The result of that would be that if the Treaty had entered into force one day before the end of the useful life of the plant – due to (say) the ratification of a Slovenian Parliament ignorant of the egregious implied term – then NEK would stand to earn a miniscule sum for the electricity it could deliver within that day, and HEP would stand to receive a vast sum, say a billion Euros if one makes it proportional to the present claim, for more than 20 years of non-delivered electricity. An absurd example? Perhaps, but how about ten years? Five? Where is any line of principle? It is sufficient to state this proposition, and its consequence, to see how implausible it is as an interpretation of the Treaty.

53. In addition, it is curious to posit a breach which could be rendered nugatory simply by non-ratification (a course of action that is agreed by all was open to Slovenia, consistent with elementary rules of international law). The ratification of the Treaty was controversial in Slovenia. How much more controversial would it have been had the Slovenian Parliament been told that the act of ratification would instantly create a State liability in the tens of millions of euros? If that consideration had delayed ratification, the notional debt would have

continued to grow, making it ever less likely that Slovenia would ever ratify. The analysis is not advanced by speculating that the Slovenian Parliament felt that accepting this liability was an acceptable price for achieving a settlement, for it is equally plausible that the Croatian Parliament felt that absorbing higher costs of alternative power purchases during the delay pending entry into force (assuming such costs were indeed higher) was the price for achieving the same settlement.

54. The paradoxes do not end there. The subtext of HEP's case, and of the majority's reasoning, is that Slovenia should pay the price for its Parliament's slowness in ratifying the Treaty. But consider the hypothesis that Croatia rather than Slovenia acted "late", and that as a result entry into force occurred only toward the end of the useful life of the plant. This would mean that Slovenia assumed the risk and financial consequences of post-30 June 2002 ratification by Croatia. This seems patently unreasonable; but the majority's view would have led to the same outcome in that hypothesis. And so one would have to add another implied term, to wit that the implied obligation inferred by HEP operates only if Slovenia ratifies second. I cannot accept a reading of an international treaty which varies depending on which Contracting State ratifies first or last. That is ad-hocery, not law.

55. The majority's reading of Exhibit 3 also throws open the doors to claims by both sides under the pre-Treaty Governing Agreements, exactly contrary to the Treaty's object and purpose of settling all such claims once and for all. As noted above, the majority conclude that the reciprocal waivers in Paragraph (2) of Exhibit 3 wiped out only claims arising before 30 June 2002. Under their Decision, NEK's claims against HEP for the interim period have not been waived. If HEP can claim for the financial consequences of the interim non-deliveries, so can NEK. The Decision resuscitates the lengthy debate as to Slovenia's entitlement to take measures affecting NEK's pricing and NEK's right to adjust its prices accordingly. It is difficult to believe that in ratifying the 2001 Agreement on 3 July 2002, the *Croatian* Parliament understood by implication that there had been such an undermining of the two Prime Ministers' achievements on 19 December 2001. The vastly complex issues attendant on the independence of former Yugoslavian States would flow back full force as though there had been no meeting of the minds of the heads of the two governments.

56. For example, Article 17 refers to the extinction of NEK's obligations to contribute to decommissioning costs "as of the date of entry into force". If it had been understood that production was promised to commence 1 July 2002 (regardless of the date of the

Treaty's entry into force), this would mean that the controversial surcharge would apply to deliveries between that date and the date of entry into force. More precisely, the debate as to its applicability would be revived. This seems implausible, since the purpose of the Treaty was to put all such matters to rest.

57. As a mental exercise, one might put oneself in the position of a lawyer advising HEP in early 2003. If HEP's current claim is good, that lawyer would have said: *If you are unlucky, Slovenia will not ratify and you will be back in the fractious pre-June 2001 environment, but if you are lucky Slovenia will ratify, will instantly owe you €60 million and will simultaneously free you from all past claims.* What agreed terms could the imaginary adviser rely upon to give such advice – and what chances would he or she give to its endorsement by an international tribunal? And what would have been the reaction of the Slovenian Parliament if advised that the alternatives were as just posited?

58. Similarly, practical questions arise. NEK, as we know, offered to deliver electricity to HEP during the interim period, but on what logical basis could it have invoiced HEP on the majority's construction of the Treaty? If NEK had insisted on invoicing the modernisation and decommissioning surcharges, HEP would have been provoked by NEK's insistence on terms which HEP had so long and so vigorously resisted, and would not have paid them (just as HEP in fact rejected NEK's offers to supply electricity on this basis). Until the Treaty came into force and HEP's past claims against the Slovenian parties were waived, NEK could hardly have delivered to HEP at the prices HEP wished to pay, effectively giving up the position of the Slovenian side without any reciprocity from the Croatian side.

59. To conclude on these matters, the majority's approach invites renewed controversy over precisely the issues that the Treaty was supposed to lay to rest. Moreover, during the period between 30 June 2002 and ratification, the parties, if they had understood the Treaty as the majority now interpret it, would have had an incentive to rekindle that controversy at the time, threatening the prospect that the Treaty would ever be ratified. The practical implications of the majority's interpretation can hardly be advocated as furthering the Treaty's object and purpose.

Retroactivity

60. The reasons for my dissent have already been stated. (For the attentive reader, Paragraph 23 should be sufficient.) What follows serves only to indicate why my colleagues' attempt to rescue their preferred outcome, using the lifeline of the *Mavrommatis* case, cannot succeed.

61. It is an elementary rule of customary international law that international agreements do not operate retroactively in the absence of a stipulation to that effect. Article 28 of the VCLT was intended to be declaratory of customary law, and has since been recognized as such; citations are hardly necessary. It provides:

> *Non-retroactivity of treaties*
>
> *Unless a different intention appears from the treaty or is otherwise established, its provisions do not bind a party in relation to any act or fact which took place or any situation which ceased to exist before the date of the entry into force of the treaty with respect to that party.*

This is why, when a treaty as a whole is subject to ratification, it is in principle impossible to accept that *some* of its provisions have retroactive effect, unless there is a clear stipulation or other agreement to the contrary.[13]

62. In the light of the cardinal rule of non-retroactivity, what could Croatia and Slovenia have done to ensure that deliveries of electricity commence no later than 1 July 2002? Two possible solutions would have suggested themselves:

(1) To provide that Article 5(2) obligations would be applied on a provisional basis from 1 July 2002 at the latest (i.e. if the Treaty as a whole had not entered in force by that time).[14] Provisional application

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[13] See *Ambatielos, ICJ Reports 1952*, 28 at 40. As the International Court of Justice observed, *ibid.* at 43, "The ratification of a treaty which provides for ratification ... is an indispensable condition for bringing it into operation. It is not, therefore, a mere formal act, but an act of vital importance."

[14] See the examples given in the UN Handbook (note 2 above) at 42-44; Aust, *Modern Treaty Law and Practice* (2000) 139-141; and Sinclair, *The Vienna Convention on*

provisions are typically to be found in agreements envisaging immediate or timely measures.[15] The present Treaty itself provides for an obligation of immediate action prior to entry into force, in Article 2(3) regarding the conclusion of the Memorandum of Association in Exhibit 1 of the Treaty.[16]

or

(2) To provide that, once the Treaty entered into force, its provisions, or Article 5(2) specifically, would have retroactive effect from 1 July 2002.[17]

Given the existence of these well known mechanisms in international treaty practice, it is impossible to read any retroactive effect into Article 5(2) of the Treaty here.

63. A suggestion to imply into the Treaty a term that would operate retrospectively (i.e. from 1 July 2002) once the Treaty had entered into force at a subsequent time faces the same difficulties. It is accepted by the Parties here that terms cannot be implied unless the express terms of the Treaty are ambiguous or absurd *and* the term to be implied would resolve that ambiguity or absurdity in a manner consistent with the two Contracting States' manifest intent in concluding the Treaty. McNair observed[18] that certain treaties will "rightly" fail to produce a result – or at least the result contended for by one party on the basis of an implied-terms doctrine – because the Contracting States did not wish to make provision for that result. McNair's example is that of the *Peace Treaties* case, where the International Court of Justice ("ICJ") refused to read provisions in two treaties as authorizing the Secretary-General of the UN to appoint a member of a three-member commission in the stead of a state that defaulted in its obligation to make that appointment. The ICJ read the

the Law of Treaties (2nd edn, 1984) at 50 (note 60). The Energy Charter Treaty contains elaborate provisions on provisional application in Article 45.

15 See for example Article 68 of the Agreement on an International Energy Programme (Paris, 18 November 1974), (1974) 14 ILM 1. That Agreement provided for measures to deal with the oil-supply emergency of that time.

16 For a similar example see Article VIII of the 1894 Gámez-Bonilla treaty, discussed in *Case Concerning the Arbitral Award by the King of Spain, ICJ Reports 1960*, 192 at 208.

17 See, e.g. the US-Korea Utilities Claims Settlement Agreement (Seoul, 18 December 1958), UNTS No. 4702; or the Belgium-France Double Taxation Convention (Brussels, 10 March 1964), UNTS No. 8127.

18 *The Law of Treaties* (1961) 383.

treaty provisions on their face, as permitting an appointment by the Secretary-General only when the two representatives already appointed by the states failed to agree on the *third* commission member.[19] As a result, the commission could not be constituted; the States-party had not dealt with all eventualities, and had not set forth a mechanism to permit the constitution of a commission in all circumstances. As the ICJ said in a later case, "Rights cannot be presumed to exist merely because it might seem desirable that they should".[20]

64. In other words, a term may be implied only when it is clear beyond peradventure, from the overall text of the relevant instrument, its negotiating history, or its actual implementation by the parties, that *all* Contracting States would have had no hesitation to include that term if they had applied their minds specifically to the situation with which the term is to deal. No such *lacuna* appears here. As discussed throughout this Individual Opinion, the Treaty is perfectly capable of operating, and reasonably so, on the basis of its express terms.

65. The majority discuss the issue of retroactivity under the rubric "The Non-Issue of Retroactivity". While this certainly makes it clear to the reader where they want to go, I fear that calling something a non-issue does not cause it to vanish.

66. When Slovenia ratified the Treaty, the date of 1 July 2002 was in the past. Any duty to make deliveries or face monetary liability as from that date would plainly be retroactive if it did not become binding (as it could not) until ratification: retroactivity is determined by reference to entry into force, not signing.[21] Moreover,

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[19] See *Interpretation of Peace Treaties (Second Phase)* (Advisory Opinion), *ICJ Reports 1950*, 221.

[20] *South West Africa (Second Phase), ICJ Reports 1966*, 6, para. 91.

[21] As Article 28 of the VCLT makes clear, the critical date by reference to which one has to determine whether an international treaty has any retroactive character is its *actual* date of entry into force. It is legally immaterial whether the obligation in question relates to events that antedated the *signing* of the relevant treaty. One cannot say that a point in time prior to a treaty's entry in force but subsequent to its signing is prospective for the purposes of Article 28 of the VCLT. And a putative obligation tied to that point in time is no less retroactive if it was envisaged – but neither certain nor legally assured – that the treaty would have entered into force before that time. After the treaty's entry in force, the obligation can only be characterized as retrospective, not prospective.

The *Ambatielos* case (*ICJ Reports 1952*, 28 at 40) does not say otherwise. Indeed, it says the contrary. Obligations under a treaty come into being only after its entry in force, and in respect of events that occur, or are to occur, after that time – unless there is a "special clause or any special object *necessitating* retroactive interpretation" (emphasis added). The reference to a "special object" clearly points to the *Mavrommatis* case, discussed in the text below (paragraphs 70 *et seq.*).

as the majority concede, *no obligation of delivery* was defined in the Treaty. Somehow they wish to attach liability to Slovenia for not having caused NEK to do what Slovenia had not undertaken that NEK would do. This considerable feat is purportedly achieved by referring to a "financial settlement ... based on the financial facts that would flow had NEK been supplied electricity starting 1 July 2002" (para. 174).

67. This is surpassingly strange, since by the express terms of the Treaty (Article 17) the financial settlement concerned "financial relations up to the *signing*" of the Treaty – i.e. 19 December 2001.

68. It is perfectly obvious that a treaty may resolve a dispute about past events, such as responsibility for an environmental catastrophe having consequences across borders, without raising any issue of retroactivity. An event occurred, two States agreed on the terms of a settlement, and when their agreement is ratified they are bound by their promise. That is not the hypothesis here. On HEP's pleaded case, the claim is one for damages arising from Slovenia's failure to make deliveries of electricity for a nine-month period starting on 1 July 2002.[22] The proposition is that the Treaty contains a duty for Slovenia to pay for the consequences of NEK's non-delivery of electricity as from 1 July 2002. This is on any view a claim for liability arising from the breach of the obligation to supply electricity. I have already explained that no such duty to deliver electricity is to be found as of 1 July 2002. But even if it existed, it would run afoul of the non-retroactivity principle, for the following reasons.

69. In other words, to say that the primary obligation (supply of electricity) is to be considered as having been breached nine months before the Treaty's entry into force is evidently an argument that the Treaty "bind[s] a party in relation to an[] act or fact which took place ... before the date of the entry into force of the treaty with respect to that party" (Article 28 of the VCLT). That claim can therefore succeed only if it were established that under Article 5(2) there was an obligation to supply electricity starting on 1 July 2002 whether or not the Treaty had entered in force by that time.

70. The majority seem to feel that this retroactivity (which they refuse to call by its name) is necessary in order not to deprive the Treaty of its intended effect. (I have already questioned their identification of this putative intent – see Paragraph 23 above – and

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22 See Request for Arbitration, paras. 9-11; Statement of Claim, paras. 254, 260; Reply, paras. 232, 253.

will not revert to that subject here.) They refer to the *Mavrommatis Palestine Concessions* case in support. Their reliance is, with respect, misplaced. The claim in that case was that the UK, administering Palestine since 1920 (but having formally obtained a Mandate only in 1922), had in 1921 granted a concession that conflicted in part with 1914-1916 Ottoman concessions to Mr Mavrommatis; and that in so doing the UK had breached its obligations as a Mandatory under Protocol XII to the Treaty of Lausanne (which entered into force in 1924).[23] The argument was that the terms of the Mandate were "subject to any international obligations accepted by the Mandatory" (Article 11), and Protocol XII, which was such an international obligation, required observance of pre-1914 concessions. Depending on whether or not the concession had been "put into operation", the obligation of the UK would be either to put Mavrommatis' concession "into conformity with the new conditions" or to "dissolve" it and pay compensation (Articles 4 and 6 of Protocol XII).

71. The majority rely on a passage from the PCIJ *Jurisdiction* decision which is quoted in the International Law Commission's commentary on the draft text for the 1969 diplomatic conference for the VCLT.[24] The PCIJ held that the "the rights recognised" in Protocol XII were "most in need of protection" in the period immediately after the restoration of peace. It was on that basis that the Court concluded that such protection was available even before the Protocol's entry in force. The import of this passage becomes clear when one reads it in context; its meaning is simply not that ascribed to it by the majority Decision:

- The main provision of Protocol XII, Article 1, stated that "concessionary contracts ... duly entered into before ... 1914 [by] the Ottoman Government ... *are* maintained" (emphasis added). As the Court held (at p. 27), the essential purpose of Protocol XII was to preserve pre-existing concessions. Preservation of pre-existing concessions was the very subject-matter of Protocol XII; and to permit a successor state to terminate such a concession before the entry in force of the Protocol would effectively defeat its entire purpose.

- To achieve this goal, Article 9 of Protocol XII had an explicit provision to the effect that in territories which were detached from Turkey by virtue of the Treaty of

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23 LNTS No. 707.

24 See [1966-II] YBILC 212.

Lausanne (which territories included Palestine), the successor state was to be subrogated to the obligations of the Ottoman Empire "as from the 30th of October, 1918". Article 9 was expressly relied upon by the Court in its judgment on the merits[25] where it found against the UK on this point. So there was an explicit element of retroactivity in the applicable international instrument at issue in *Mavrommatis*, which is absent in the Treaty here.

– Though Protocol XII entered in force in 1924, after the Mandate had formally been given in 1922, the draft text of the Mandate had envisaged a provision requiring preservation of pre-1914 concessions (see pp. 24-25 and 36 of the judgment). The UK was aware of that obligation in accepting the Mandate.[26]

72. In short, the subject-matter of Protocol XII to the Treaty of Lausanne was preservation of acquired rights. That is the very opposite of the prospective obligation to supply electricity under the Treaty here. There is no plausible analogy between *Mavrommatis* and the present case. Retroactivity is not necessary to the object and purpose of the Treaty. The Treaty is perfectly capable of operating in full without reading the date of 1 July 2002 into Article 5(2).

73. Moreover – and this strikes me as fundamental – (i) if the date of 1 July 2002 were an essential ingredient of the "financial settlement" *between the two Contracting States*, and (ii) that settlement is an essential – indeed, self-standing – term of the Treaty, without which the Treaty as a global bargain makes no sense, and (iii) if the 1 July 2002 date cannot, for objective reasons, be met, then (iv) the consequence would not be a cause of action accruing to HEP but an inter-State claim for revision or termination of the Treaty. No such claim has been made or apparently ever envisaged.

74. At their para. 201 the majority reason that the expression "otherwise established" in Article 28 VCLT allow them to look at the "intention" that flows from "the very nature" of the Treaty. This

[25] Series A, No 5 (1925). At p. 39: "The obligation accepted by the Mandatory to maintain concessions governed by the Protocol is therefore to be regarded, by virtue of this clause [Article 9], as having existed at the time the Rutenberg concession [competing with the Mavrommatis concession] was granted."

[26] The Mandate would be subject to the Treaty of Sèvres (signed August 1920, never in force), Article 311 of which was to effect similar with that of Protocol XII to the Treaty of Lausanne.

seems to be an almost mystical suggestion that any tribunal may do what it pleases by referring to "the very nature" of a Treaty instead of to its terms. It does not strike me as acceptable legal scholarship. The ILC commentary to the draft text for the 1969 diplomatic conference (from which my colleagues quote at para. 197 and from which they borrow the *Mavrommatis* quotation) said this:[27]

> *The general phrase "unless a different intention appears from the treaty or is otherwise established" is used in preference to "unless the treaty otherwise provides" in order to allow for cases where the very nature of the treaty rather than its specific provisions indicates that it is intended to have certain retroactive effects.*

The example given by the ILC as one of a treaty "having a ... 'special object' necessitating retroactive interpretation" is none other than *Mavrommatis*.[28] One could scarcely think of a better way of underscoring *Mavrommatis'* inappositeness here.

HEP's standing under the Treaty

75. As indicated in Paragraph 3 above, the curiosity of HEP's claiming under the Treaty, although a non-party to it, was not a matter of fundamental concern in terms of my determination that I would express dissent, for the simple reason that it was not a key feature of the Parties' debate. But having seen paras. 166-169 of the majority's Decision, concluding with the affirmation that they are "in no doubt" as to their jurisdiction to resolve "the dispute here presented" (i.e. as presented by HEP as claimant), I cannot assent. Para. 168 contains the majority's only reasoning on this point. It simply does not address the issue of HEP's standing. The words "In doing so" that introduce the fourth sentence of para. 168 is yet another *non sequitur*. The fact that the Treaty contains a number of elements that are frequently to be found in shareholders' agreements may or may not make it convenient that corporate entities like HEP should, under the Treaty, be given the right of direct action before ICSID. But where does the Treaty say that the States-party so agreed? Where is the evidence that Article 25(1) of the ICSID Convention is satisfied to the effect that "the parties to the dispute", i.e. HEP and Slovenia, have given "consent in writing to submit to the Centre"?

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27 [1966-II] YBILC 212-213.

28 See *ibid* 212.

Conclusions

76. I cannot concur in the conclusions reached by the majority, and therefore naturally disassociate myself from the *dispositif* they have proposed, particularly the portion set out in paragraph 202(A) of their Decision. Specifically:

- Subparagraph 202(A)(i) declares that Article 17(1) and Exhibit 3 of the Treaty constitute a financial settlement "as of 30 June 2002", a conclusion that is contradicted by the two cited parts of the Treaty, perhaps most starkly by Article 17(1): "Mutual financial relations existing *up to the signing of this Agreement* ... shall be regulated in accordance with the principles set forth in Exhibit 3 of this Agreement" (emphasis added).

- Subparagraph 202(A)(ii) imposes liability on Slovenia (subject to further proceedings) for non-delivery of electricity after 30 June 2002. As I have stated, I cannot see anything in the Treaty imposing on Slovenia either an obligation to procure delivery between 30 June 2002 and the Treaty's entry into force or to compensate Croatia (let alone HEP) for non-delivery. It is in my view telling that the *dispositif* cites two parts of the Treaty as the basis for Slovenia's liability (Article 17(1) and Exhibit 3) but does not cite the only Treaty provision that actually mentions, let alone imposes, a delivery obligation, namely Article 5.

- The remaining subparagraphs of the *dispositif* track, nearly verbatim, the subparagraphs of Exhibit 3, Paragraph (2) of the Treaty. These are the subparagraphs that spell out the specific claims that have been waived by virtue of that Paragraph in Exhibit 3. The only significant difference between the texts of the Treaty and the Decision is the majority's addition, in each subparagraph, of a phrase to the effect that claims have been waived "from the beginning of time through 30 June 2002". This is a radical rewriting. Why 30 June 2002? Surely if there is no date in the

Treaty text, the most plausible date is that of entry into force. That plausibility becomes certainty when one sees the words at the beginning of Paragraph (2) that do *not* appear in the *dispositif*: the parties waive all claims "by virtue of the entry into force of this Agreement".

[*signed*]

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Jan Paulsson
8 June 2009