

*This case summary was prepared in the course of research for
[S Ripinsky with K Williams, Damages in International Investment Law \(BIICL, 2008\)](#)*

Case summary

Československá Obchodní Banka, A.S.
V
The Slovak Republic

Year of the award: 2004

Forum: ICSID

Applicable law: Consolidation agreement, Czech law, Czech-Slovak BIT (1992)

Arbitrators	Timeline of the dispute
Prof. Hans van Houtte – President Prof. Piero Bernardini Prof. Andreas Bucher	18 April 1997 – notice of arbitration 20 August 1997 – arbitral tribunal constituted 24 May 1999 – first decision on jurisdiction 1 December 2000 – second decision on jurisdiction 29 December 2004 – arbitral award

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I. Executive Summary

Československá Obchodní Banka, A.S. (CSOB), a Czech commercial bank, brought a dispute against the Slovak Republic before an ICSID Tribunal, claiming the breach by the Slovak Republic of the so-called “Consolidation Agreement” and approx. US\$ 1.4 billion in damages. The Consolidation Agreement was concluded in 1993 by the Czech Republic, the Slovak Republic and CSOB in order to carry out the Bank’s financial restructuring in advance of its then planned privatization.

Under the Agreement, the Czech Republic and the Slovak Republic each established a special-purpose collection company to which CSOB assigned certain non-performing receivables. To enable the collection companies to pay for the assigned receivables, CSOB extended to each of them a loan facility in an amount equal to the nominal value of the non-performing loans that had been assigned.

As the non-performing loans assigned to the collection companies were not expected to generate revenues sufficient to satisfy the collection companies’ loan obligation to CSOB, in the Consolidation Agreement the Czech and the Slovak republics each agreed to “cover any losses” of the respective collection companies. The Slovak Republic, however, failed to cover these losses, with the Slovak collection company consequently defaulting on its loan obligations to CSOB.

In the award, the Tribunal determined that the applicable law in this dispute comprised, in addition to the Consolidation Agreement, Czech law (chosen by the parties in the Agreement) and the Czech-Slovak BIT, also referred to in the Agreement. In fact, the Claimant invoked the BIT only to have resort to ICSID arbitration.

The Tribunal established that the Slovak Republic indeed breached the Consolidation Agreement by failing to cover losses of the Slovak collection company and consequently of the CSOB. The Tribunal awarded compensation of approx US\$ 867 million comprising the loan not repaid to CSOB, interest due under the loan contract as well as interest under the Czech law. The Tribunal also awarded US\$ 10 million in arbitration costs in favour of the Claimant.

The award has quite limited value for future disputes under BITs and other investment treaties as neither BIT rules, nor general international law rules were applied by the Tribunal and no relevant legal interpretations were developed.

II. Factual Background and Claims of the Investor

The Claimant, Československá Obchodní Banka, A.S. (CSOB), is a commercial bank organized under Czech law. It brought a dispute against the Slovak Republic before an ICSID Tribunal claiming damages that had arisen because of the Repondent’s alleged failure to perform its obligations under the “Consolidation Agreement”, which included a reference to the Czech-Slovak BIT and its investor-State dispute settlement provision.

The Consolidation Agreement was a contract concluded in 1993 among the Czech Republic, the Slovak Republic and CSOB in relation to the Bank's financial restructuring in advance of its then planned privatization. Like many other financial institutions in formerly non-market economies, CSOB required financial restructuring in order to remain solvent and competitive as the Czech and Slovak economies evolved from to a market system. To this end, in accordance with the Consolidation Agreement, the Czech Republic and the Slovak Republic each established a special-purpose collection company to which CSOB assigned certain non-performing receivables. Pursuant to the Consolidation Agreement, CSOB extended a loan facility to each of the collection companies in an amount equal to the nominal value of the non-performing loans that had been assigned. Uncertain receivables were thus removed from CSOB's balance sheet and were replaced by payments made by Czech and Slovak collection companies, financed with funds provided as a loan by CSOB.

One of the essential features of the assignments and their financing was that the Czech Republic and the Slovak Republic had agreed in the Consolidation Agreement to "cover any losses" of the collection companies, as the non-performing loans assigned to these companies were not expected to generate revenues sufficient to satisfy the collection companies' loan obligation to CSOB.

CSOB claimed that the Slovak Republic failed "to cover the losses" of the Slovak collection company. The Slovak collection company consequently defaulted on its loan obligations to CSOB and later was subjected to bankruptcy proceedings.

CSOB claimed losses of around 40 billion Slovak Crowns (approx. US\$ 1.4 billion) consisting of the loans not repaid to it by the Slovak collection company, interest, lost profits and costs. All CSOB claims were based on the Consolidation Agreement, and not on the Czech-Slovak BIT. The latter served only as a procedural tool to submit the dispute to international arbitration.

III. Findings on Merits¹

A. Applicable law

As said above, CSOB's claims were based on the Consolidation Agreement concluded between the Czech Republic, the Slovak Republic and CSOB. The parties submitted the Consolidation Agreement to Czech law, which was extensively applied by the Tribunal. The Consolidation Agreement also contained a reference to the Czech-Slovak BIT which had the effect of submitting disputes arising under the Consolidation Agreement to ICSID arbitration. Therefore, the Agreement itself, Czech private law and the BIT constituted applicable law in this dispute.

Concerning the application of international law, the Tribunal determined that the Consolidation Agreement was not a treaty between States governed by international

¹ Before proceeding to the merits of the dispute, the Tribunal addressed the Slovak's Republic's jurisdictional challenges. See the Tribunal's decisions on jurisdiction of 24 May 1999 and of 1 December 2000.

law (para.59) and decided that international law was generally not applicable except to the extent that it was relevant for the interpretation of the BIT. (para.63)

B. Obligation to Cover Losses under the Consolidation Agreement

As the assigned receivables were non-performing, it was clear that the collection companies would not be able to recover the full nominal value of the assigned receivables which would have allowed the repayment of the loan to CSOB. Therefore, in Article 3 of the Consolidation Agreement the Slovak Republic undertook to cover “any losses” made by the Slovak collection company, “including payment of interest”.

Upon examination of this “cover losses” provision of the Consolidation Agreement, the Tribunal concluded that this provision identified adequately and in a definite and understandable manner the Slovak Republic’s obligation to cover losses of the collection company as soon as and to the extent that the recovery of the assigned receivables did not allow to repay CSOB’s loan. (para.155)

The Slovak Republic argued, *inter alia*, that the “cover losses” provision of the Consolidation Agreement was undertaken in relation to the Slovak collection company; it did not have CSOB as beneficiary. The Tribunal determined, however, that although it was true that the “cover losses” provision did not mention CSOB explicitly, the Slovak Republic’s “cover losses” obligation could make sense only if it entitled CSOB to claim from the Slovak Republic its losses, otherwise CSOB would be deprived for any meaningful protection for its loan – this would in turn breach the Slovak Republic’s commitment to let CSOB “enjoy full protection and security” as provided for in Article 2(2) of the BIT. Therefore, the Tribunal rejected the Slovak Republic’s contention that CSOB had no title to claim under the “cover losses” provision of the Consolidation Agreement.

The Tribunal found that the Slovak Republic failed to respect its obligation to cover losses in a way that allowed the repayment of the loan, and that CSOB’s damage was caused by the Slovak Republic’s breach of its “cover losses” obligation.

IV. Findings on Damages

A. Law Applicable to the Determination of Damages

As far as the determination of CSOB’s damages is concerned, the Tribunal applied the Consolidation Agreement as well as relevant provisions of Czech law.

B. Compensation

The Tribunal determined that under Article 3 of the Consolidation Agreement, to the extent that the Slovak collection company was not in a position to repay the CSOB’s

loan and therefore made a loss, the Slovak Republic was required to compensate for such loss.

The Tribunal proceeded to consider and estimate the different heads of damages claimed by CSOB under the Consolidation Agreement and Czech law:

- The principal amount of CSOB's loan to the Slovak collection company and not repaid (awarded);
- Interest as provided for in the loan agreement (awarded);
- Lost profits – money that CSOB would have earned by investing the loan funds, had the latter been returned in time (dismissed for lack of evidence of the alleged high profit margins);
- Interest under Czech law on the CSOB's damages claim starting from 1997 (when the principal amount and interest became due) until the date of the award (awarded);
- Post-award interest (awarded).

In making its award of damages, the Tribunal did not refer to rules of international law and thus did not develop any relevant legal interpretations. Valuation methods were also not required in this case, as no valuation of assets or of lost profits was necessary.

In total, the Tribunal awarded the compensation of 24.8 billion Slovak Crowns (approx. US\$867 million).

C. Costs

CSOB requested compensation for all the costs and expenses of the arbitration proceedings in the amount of US\$ 16.3 million. The Tribunal decided to award US\$ 10 million, taking into account that the Slovak Republic opposed without success the Tribunal jurisdiction, that its objections on the merits were rejected by the Tribunal whereas CSOB's claim for compensation was granted in the prevailing part.