International Centre for Settlement of Investment Disputes (ICSID)

COMPAÑÍA DEL DESARROLLO DE SANTA ELENA, S.A.

v.

THE REPUBLIC OF COSTA RICA Case No. ARB/96/1

CASE ANALYSIS

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Introduction

This case note will analyse an international arbitration that took place before the ICSID in the late 1990s. In *Compañía del Desarrollo de Santa Elena, S.A. v. The Republic of Costa Rica*¹ the Tribunal had to decide whether or not Costa Rica had offered a sufficient compensation for the expropriation of a group of U.S. investors. The property at stake spanned across 40,000 acres and was located in the north of Costa Rica. It was acquired by a group of American investors in the early 1970s. The investors intended to develop the site into a tourist resort; its plans were halted by the Costa Rican government, which expropriated them in 1978. The expropriation decree was issued in an attempt to preserve the Santa Elena property’s unique flora and fauna as evidenced by its recognition as a UNESCO World Heritage Site in 1999. Whilst the claimants did not challenge the expropriation itself, the compensation offered by Costa Rica was deemed insufficient to make up for the potential future revenues a tourist development project would have provided for.

The arbitral dispute has gained considerable prominence both in academic literature² as well as subsequent arbitration practice³ for two reasons. First, it broaches some of the most fundamental principles of international (investment) law, such as the standard of investor protection in the absence of a BIT and the general principles of valuation. Second, there was very limited precedent at the time of the proceedings as to how a state’s legitimate interest in protecting the environment can be balanced with the protection of investors under the existing legal framework. As this case note will show, the ICSID Tribunal was reluctant to attribute special relevance to the objective of environmental protection. Thus, the ruling was criticised for turning a blind eye on the increasing efforts on the international level to make environmental protection a common objective.⁴

⁴ See below 3.1.
Besides the salient legal questions the Tribunal had to address in the Award, it is important to understand some of the political issues underpinning this dispute. Brower and Wong, a judge and an academic, suggest that the Santa Elena property was used for clandestine CIA flights in the 1970’s in order to deliver supplies to the “Contras”\(^5\). In 1978 when the investors were expropriated, tensions between the United States and many Central and Latin American countries peaked. Whilst the dispute was only settled in 2000 – long after the Cold War had come to an end – the intricate diplomatic and political situation at the time of the expropriation must not be forgotten in order to better understand the full picture.

Having said this, the case note will not engage in speculation but put its focus on the legal problems addressed by the Tribunal. Chapter 1 will outline the key facts underpinning this dispute. It will cover the circumstances under which the Santa Elena property was purchased by the foreign investors, the content and the nature of the expropriation decree issued by the government of Costa Rica as well as the various domestic lawsuits which preceded the arbitral dispute before the ICSID. Chapter 2 will then focus on the proceedings before the ICSID Tribunal and closely analyse the decision. For this purpose Chapter 2 will review jurisdictional issues, examine the law applicable to the dispute, assess and discuss the standard of investor protection and analyse the Tribunal’s decision regarding the amount of compensation Costa Rica was required to pay. In Chapter 3 this note will take a closer look at the central issue at stake. How did the Tribunal balance Costa Rica’s objective of protecting the unique Santa Elena site with the protection of investors from expropriation? As Chapter 3 will illustrate, the Tribunal did not establish new legal concepts in international investment law despite some scholars having long demanded a more balanced approach to environmental protection in ICSID arbitration cases.

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\(^6\) A group of rebels that fought the Nicaraguan government.
1. Facts of the Case

1.1. Acquisition of the disputed property

The property subject to this arbitral dispute – referred to as Santa Elena – is located in Costa Rica’s Guanacaste province in the northwest of the country. As mentioned above, the site is unique from an ecological point of view, consisting of numerous rivers, springs, valleys and forests, which are home to a dazzling variety of flora and fauna. The Santa Elena property was purchased in 1970 by a Costa Rican company incorporated under the name Compañía del Desarrollo de Santa Elena, S.A. (hereinafter “CDSE”), which was owned by U.S. citizens. The U.S. investors founded this company under Costa Rican law for the purpose of legally acquiring the Santa Elena property and develop it into a tourist resort and a residential community. The purchase price of the property amounted to roughly $395,000. Soon after the acquisition was completed CDSE started to design a land development project and undertook various valuations with respect to the best possible use of the land for business purposes. Yet, before CDSE could realise these plans the Costa Rican government stepped in. Thus, the investment made by the foreign investors was limited to the purchase as well as planning and designing activities. As we will see later, this is important as the compensation claimed by CDSE exceeded the actual amount invested by a multiple.

1.2. The Expropriation Decree

On 5 May 1978 the government of Costa Rica issued a decree against CDSE to the effect that the company lost ownership rights of large parts of the Santa Elena property. In justifying the decision to expropriate CDSE, the government held that “…the National Park (bordering Santa Elena) contains flora and fauna of great scientific, recreational, educational, and tourism value, as well as beaches that are especially important as spawning grounds for sea turtles”. Thus, the decree argued that “…the current area of the Santa Rosa National Park...”.

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7 CDSE v. Costa Rica, supra note 1, at 15.
8 Id.
9 Id, at 16.
10 CDSE v. Costa Rica, supra note 1, at 16.
11 Id.
12 Id, at 18.
is insufficient to maintain stable populations of large feline specie and substantial area needs to be added to carry our its conservationist objectives”. Based on these environmental concerns the government considered it necessary to expropriate CDSE before it started any commercial development activities. According to the official decree, the investors accepted Costa Rica’s action and refrained from challenging the legality of the act as such. However, it quickly became clear that the compensation of approximately $1,900,000 offered by the government was deemed inadequate by CDSE. The divergent views on the adequate valuation of the property formed the basis for the dispute before the ICSID Tribunal 22 years later. In response to the expropriation CDSE demanded more than triple the amount the government was willing to pay (approx. $6,400,000). Interestingly though, CDSE later demanded a considerably higher payment in the course of the proceedings before the ICSID, hoping to recover the property’s value as of the year 2000.

Despite the unambiguous expropriation order, CDSE actually retained title to Santa Elena. CDSE kept contesting the compensation offered by Costa Rica was inadequate and reserved its right to dispute the price before a court. As the government was reluctant to take any physical actions to remove the owners from the property, the expropriation decree became invalid in 1987. This was due to a Costa Rican law, which obliges the government to dedicate the expropriated land to a public purpose within 10 years. However, instead of granting title to CDSE again, Costa Rica issued another expropriation decree that went even further than the first one. It expanded the boundaries of the Santa Rosa National Park to include the entire Santa Elena in order to forestall the automatic invalidation of the 1978 decree. This rendered the development of a tourism resort once and for all impossible.

1.3. Lawsuits Before Municipal Courts

Following the expropriation in May 1978, CDSE challenged the official order in various domestic courts. The case went all the way up to the Costa Rican Supreme Court, but was

13 Id.
14 Brower/Wong, supra note 3, at 3.
15 Id.
16 CDSE v. Costa Rica, supra note 1, at 22.
17 Brower/Wong, supra note 3, at 4.
unsuccessful.\textsuperscript{18} CDSE also countered the 1987 Decree by seeking an annulment before Costa Rican courts, arguing that the decree amounted to a \textit{de facto} expropriation.\textsuperscript{19} Again, the courts threw out CDSE’s challenges. Offering $4.4 million of compensation in its second decree, Costa Rica moved closer towards $6.4 million CDSE had initially demanded. Yet neither party was willing to agree to a compromise. Absent a Bilateral Investment Treaty or any other legal obligation to refer the dispute to an international tribunal, domestic litigation appeared to be the only viable path for CDSE to challenge the decision. The ICSID award itself has not provided much information on the course of these proceedings and whether or not they were conducted in a fair and equitable manner. It made clear however that the intense litigation led to a delay in the arbitration proceedings and – as we will see later – exacerbated the prospects of retrospectively assessing the true and fair value of the property. Whilst the parties launched several attempts to settle the dispute in the 1990’s, in and out of court, a compromise appeared highly unrealistic. This changed in 1994 when the U.S. policy on foreign aid became more hawkish. The next section will explain how the enactment of a new law, referred to as the “Helms Amendment”, strongly influenced Costa Rica’s decision to agree to a settlement before the ICSID and led to the final award in 2000.

1.4. The Helms Amendment

The Helms Amendment – as laid out in U.S. Code Title 22 § 611 – played a vital role in persuading Costa Rica to submit the \textit{Santa Elena} dispute to the jurisdiction of the ICSID. Absent any contractual arrangements (such as BITs), dispute settlement before an international tribunal was dependent on Costa Rica’s voluntary submission. The Helms Amendment, named after the U.S. Senator Jesse Helms, essentially prohibited U.S. foreign aid to a country that had expropriated the property of a U.S. citizen or a corporation at least 50% owned by U.S. citizens under certain circumstances. Such prohibition would also be applicable if the expropriating country had not provided effective compensation required by international law and not submitted the dispute to arbitration under the rules of the ICSID Convention.\textsuperscript{20} Following Costa Rica’s 1987 expropriation decree, CDSE pressured the U.S. government to invoke this Amendment against Costa Rica as a response to the insufficient

\textsuperscript{18} \textit{Id.}

\textsuperscript{19} \textit{Id.}

\textsuperscript{20} \textit{CDSE v. Costa Rica, supra} note 1, at 24.
compensation offered.\(^{21}\) As a result, the U.S. State Department blocked a $175 million Inter-American Development Bank loan to Costa Rica in 1995. This blow came at a time when Costa Rica found itself in a devastating economic condition with inflation levels of more than 20% and the highest debt to GDP ratio in Central America.\(^ {22}\) Unsurprisingly, the Costa Rican government ultimately complied with CDSE’s demands to take the dispute before the ICSID through a letter to the Tribunal stating its consent on 21 March 1995.\(^ {23}\)

2. Proceedings before the ICSID

2.1. The Written and the Oral Phase of the Proceedings

As discussed above, the Claimant did not call into question Costa Rica’s right as a sovereign nation to expropriate property owned by foreigners for a public purpose. CDSE rather disagreed with the amount of compensation offered and the way Costa Rica had calculated it.

2.1.1. The Claimant’s Position

CDSE stated that the main purpose of the arbitration was to determine the compensation owed and therefore the correct valuation of the Santa Elena property. Such adequate calculation of the value was to be done in accordance with Costa Rican law. CDSE argued that Costa Rican law complied with the rules of international law related to the issue compensation.\(^ {24}\) Hence, as the “default law” under Art 42(1) ICSID Convention, it had to prevail over international law. Whilst it seems surprising at first glance that CDSE favoured Costa Rican law over international law, a closer look solves the puzzle. According to Costa Rican law, the valuation of the property must be based on the current fair market value (i.e. the property’s value in the year 2000) rather than the 1978 value.\(^ {25}\)

International law on the other hand, stipulates that the decisive moment for determining the value of the property is the date when the expropriation is consummated (i.e. in 1978). CDSE justified this by arguing that there is no conflict between Costa Rican and international law.

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\(^{21}\) Id.  
\(^{24}\) Id.  
\(^{25}\) Id, at 35.
and that the parties had never agreed on any other contractual or statutory regime governing the relationship. Consequently, Costa Rica should be ordered to reimburse the current fair market value of $41,200,000. This enormous sum exceeded the demands made in 1978 by about $35 million. It was based on an appraisal made by Mr. Landauer, a private expert. He concluded that the highest and best use that was possible, legally permissible and financially feasible was the development of a tourism resort as intended by CDSE. Based on a calculation of discounted future cash flows resulting from the orderly sell-off of six resorts located inside the Santa Elena property, CDSE could have made a total revenue of at least $41 million.

2.1.2. The Respondent’s Position

In its submission Costa Rica defended its actions vis-à-vis CDSE between 1978 and the date of the arbitration. It emphasised that by expropriating CDSE in a non-discriminatory fashion, for a public purpose and accompanied by provision for prompt, adequate and effective compensation, it had obeyed the pertinent rules of international law. Costa Rica however, evaded both the question of whether or not municipal law or international law was to be applied and the related question of whether or not there was a divergence between the two legal systems with respect to the valuation. Costa Rica also vehemently opposed CDSE’s position on the valuation of the property and Mr. Landauer’s appraisal. It argued that various obstacles to large-scale commercial development imposed by Costa Rican environmental law would have negatively affected the property’s market value.

Furthermore, Costa Rica contended that international treaties the country had ratified, such as the 1992 Convention on Biological Diversity and the Central American Regional Convention for the Management and Conservation of the Natural Forest Ecosystems, would

26 Id, at 45.
27 Brower/Wong, supra note 3, at 13.
28 CDSE v. Costa Rica, supra note 1, at 40.
29 Brower/Wong, supra note 3, at 14.
oblige it to constrain tourism development projects.\textsuperscript{32} This holds particularly true for the Santa Elena property, which was listed under the World Heritage Convention.\textsuperscript{33} Against this background, the Landauer appraisal was flawed as it ignored Costa Rica’s environmental obligations at the international and domestic level. Costa Rica therefore retained the view that the compensation of approximately $1.9 million was in line with the property’s value at the time of the expropriation and that there was no reason for CDSE not to accept it.

\section*{2.2. The Tribunal’s Decision}

\subsection*{2.2.1. Jurisdiction}

The first question to be decided by the Tribunal was the one on jurisdiction. According to Article 25 paragraph 1 of the ICSID Convention the Centre has jurisdiction when the parties to the dispute consent in writing to submit to the Centre. Thus the ICSID’s competence to render a binding ruling is first and foremost dependent on the voluntary consent of both parties. Although Costa Rica was reluctant for almost two decades to submit the dispute to the ICSID both parties had submitted valid written statements by March 1996 declaring their consent to have the dispute settled under the rules of the ICSID Convention.\textsuperscript{34} As outlined above, Costa Rica’s consent was mainly due to economic pressure from the U.S., which threatened to block vital development aid to Costa Rica. Whilst coercive measures to establish the ICSID’s jurisdiction might void the voluntary consent given by one party, blocking foreign aid is a diplomatic and therefore political tool often applied in the field of international relations.\textsuperscript{35} Hence, jurisdictional questions were quickly cleared up and the Tribunal proceeded to address the key point of disagreement between the parties – the applicable law.

\subsection*{2.2.2. Applicable Law}

The question of what law the ICSID Tribunal had to apply was the focal point of the arbitration. Ascertaining whether Costa Rican law, as argued by the Claimant, or

\begin{footnotesize}
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\item \textsuperscript{32} Brower/Wong, supra note 3, at 14.
\item \textsuperscript{33} Id, at 15.
\item \textsuperscript{34} CDSE v. Costa Rica, supra note 1, at 26.
\item \textsuperscript{35} Compare e.g. Lynne Dratler Finney, Development Assistance--A Tool of Foreign Policy, 15 Case W. Res. J. Int'l L. 213 (1983), at 214.
\end{itemize}
\end{footnotesize}
international law, as argued by the Respondent, was applicable had a direct and significant impact on the amount of compensation. As explained below, this difference derives from the point in time at which the valuation ought to take place under the rules of the respective legal system.

To reach a decision, the Tribunal first turned to Article 42 (1) of the ICSID Convention for guidance. This provisions stipulates that the Tribunal has to decide a dispute (a) in accordance with the law as agreed by the parties and – in the absence of an agreement – (b) in accordance with the law of the Contracting State party to the dispute and (c) the rules of international law as may be applicable. As the parties did not agree on any other legal regime to govern their legal relationship with respect to CDSE’s investment in Santa Elena, the Tribunal had to ascertain whether municipal or international law was applicable to the dispute. As Bower and Wong point out, the prevailing view was that the Contracting State’s law (herein Costa Rican law) was the “default law”.36 According to many scholars37, the rules of international law either had a corrective function, provided the national law did not conform to international law or a supplementary function, serving as a “lacuna” when the Contracting State’s law was incomplete.38 Hence, if the Contracting State’s rules on expropriation of (foreign owned) property did not align with the pertinent rules of international law, the latter must prevail to ensure uniform and equitable investor protection.

In a first step, the Tribunal in the Santa Elena case noted that the rules and principles of Costa Rican law were generally in accordance with accepted principles of international law.39 It stressed however that any inconsistency renders international law the prevailing and thus applicable legal regime.40 The Tribunal found that international law also has a “controlling” function.41 It did not however specify whether the controlling function is to be understood as

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36 Bower/Wong, supra note 3, at 11.
39 CDSE v. Costa Rica, supra note 1, at 64.
40 Id.
41 Id.
a subcategory of the well-established corrective and complementary functions of international law according to Article 42(1) ICSID Convention, or as a separate third category. Whilst this question can be left open, the Santa Elena award underscores the ICSID’s objective of ensuring uniform standards of international investor protection.

The Tribunal presiding over the Santa Elena case pointed out two specific reasons why the rules of international law were applicable: First, due to the particular circumstances in which the dispute was submitted to arbitration and in which the parties’ consent was given. Second, due to the vital role the Helms Amendment played in persuading Costa Rica to submit the dispute to arbitration. In the Tribunal’s view the Helms Amendment’s language (“compensation...as required by international law”) reinforces the applicability of international law in this expropriation case. In addition, the Tribunal held that failing to apply the principles of international law in cases involving the takings of property would frustrate the purpose of the ICSID Convention.

2.2.3. Standard of Investor Protection

After the question of governing law was resolved, the Tribunal had to ascertain the level of protection international law bestows upon the foreign investor. As emphasised above, both parties agreed that an expropriation of property by an official decree – lawful or not – warrants the payment of compensation. Neither party challenged Costa Rica’s right to expropriate foreign investors’ property for a legitimate public purpose. Essentially two questions remained: First, does the nature of the public purpose (here environmental) affect the amount of compensation due? Second, should the legal constraints on the investor’s ability to develop a business be taken into account? In other words, does the compensation payable under international law include the loss of future profits? As the second question is closely intertwined with more general questions of how to value the property, it will be analysed in greater detail below.

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42 Id.
43 Id., at 66.
44 Id.
45 Id., at 64.
46 See below 2.2.4.
With respect to the first question, Costa Rica stressed its longstanding commitment to protecting the environment as well as the special status of the Santa Elena property as a U.N. World Heritage site. Yet the Tribunal rejected the government’s claims that this commitment would affect its obligations under international investment law. The panel rather noted that the “purpose of taking the environment does not alter the legal character of the taking for which adequate compensation must be paid.” It also held that “the international source of the obligation (to protect the environment) makes no difference” and that “environmental expropriatory measures – no matter how laudable and beneficial to society they may be – are similar to any other expropriatory measures”.

The Tribunal did not elaborate further on environmental protection and its relation to international investment law. This – arguably controversial – approach was in line with the reasoning in Southern Pacific Properties v. Arab Republic of Egypt. This seminal arbitration, which I will come back to in Part 3, was the leading case at the time with respect to direct expropriations to protect cultural heritage from tourism development projects.

2.2.4. Compensation and Valuation

First the Tribunal noted that the vocabulary describing the amount of compensation payable for a lawful taking contains words such as “full”, “adequate”, “appropriate”, “fair” and “reasonable” compensation. Furthermore, it held that the expropriating state was usually obliged to pay the “market value” based on the “highest and best use” of the property, i.e. what a willing buyer would pay to a willing seller. However, to establish the fair market value of the property, the Tribunal needed to specify the date that the valuation should have taken place. As mentioned before, the value of the property has – at least in the Claimant’s view – significantly increased over the past two decades.

47 CDSE v. Costa Rica, supra note 1, at 71.
48 Id.
49 In Part 3 I will show how practitioners and academics responded to the Tribunal’s decision not to elaborate on the question as to how environmental concerns ought to influence the level of compensation payable by the expropriating state.
50 ICSID Case No. ARB/84/3, Final Award (20 May 1992).
51 Id, at 69.
52 Id, at 73.
For this purpose the Tribunal held that under international law a property has been expropriated “when the effect of the measures taken by the state has been to deprive the owner of title, possession or access to the benefit and the economic use of his property”.\textsuperscript{53} This view is based on earlier decisions by arbitration tribunals, such as the arbitration case \textit{Tippetts, Abbett, McCarthy, Stratton v. TAMS-AFFA} \textsuperscript{54}, cited by the Tribunal in the Santa Elena Award. According to this decision, the date of the expropriation is the moment “\textit{when the owner was deprived of the fundamental rights of ownership and the deprivation is not merely ephemeral}.”\textsuperscript{55} Thus, as soon as the government’s interference has made the private right of ownership useless, the expropriation is completed and the property must be valued to determine the compensation.\textsuperscript{56} With regards to the expropriation of CDSE, the ownership was irretrievably lost at the day when the decree was issued (i.e. 5 May 1978).\textsuperscript{57}

The next step, which involved the retrospective assessment of the property’s market value, posed a considerable challenge for the Tribunal. Costa Rica’s unilateral appraisal, on which the initial compensation offer was based, was the only available evidence of what the property was worth in 1978.\textsuperscript{58} As the appraisal was the very document the dispute revolved around, the Tribunal decided to base its assessment on an approximation based on the appraisals effected by both parties and submitted to the Tribunal.\textsuperscript{59} This method has been used in previous international arbitrations such as the \textit{AIG}\textsuperscript{60} and the \textit{Philipps Petroleum}\textsuperscript{61} cases before the Iran-U.S. Claims Tribunal. From both a legal and a practical point of view determining the true value of the property by means of approximation seemed like the only viable solution in absence of an independent valuation. Tribunals in the \textit{AIG} and the \textit{Philipps Petroleum} cases argued that the assessment of the fair market value requires the

\textsuperscript{53} Id, at 76.
\textsuperscript{54} Award No. 141-7-2 (June 22, 1984), reprinted in 6 Iran-U.S. Cl. Trib. Rep. 219, 226 (1986).
\textsuperscript{55} Id.
\textsuperscript{56} CDSE v. Costa Rica, supra note 1, at 78.
\textsuperscript{57} Id, at 80.
\textsuperscript{58} Id, at 88.
\textsuperscript{59} Id, at 90.
\textsuperscript{60} American International Group, Inc. and American Life Insurance Company v. The Islamic Republic of Iran and Central Insurance of Iran (Bimeh Markazi Iran), Award No. 93-2-3, 4 Iran-U.S. C.T.R. 96 (Dec. 19, 1983).
consideration of all relevant factors and must take into account the appraisals submitted by
the parties to the dispute.

Accordingly, the Tribunal in the *Santa Elena* arbitration sought to establish a middle ground
between the parties by duly considering both views. As the Claimant had asked for $6.4
million in 1978 and Costa Rica had offered $1.9 million, the Tribunal concluded that the
actual and true fair market value has to lie between those two figures.\(^{62}\) This approximation
was based on the assumption that CDSE would have charged the highest amount possible and
Costa Rica would have paid the lowest amount it could reasonably justify. Hence, the
Tribunal decided that the golden middle, namely $4.15 million, was the fair market value of
the property in 1978 and the compensation payable by Costa Rica.

**2.2.5. Interest**

The question whether or not interest was to be paid on the compensation proved vital. This
was due to the long period between when the expropriation took place and when the decision
by the Tribunal was rendered. The Tribunal emphasised that international law generally
allows for the award of simple interest in case of injury or breach of contract.\(^{63}\) However, it
also noted that this principle ought not to be applied in cases relating to the valuation of
property or property right.\(^{64}\) Instead the expropriating state has to pay compound interest if
warranted by the special circumstances of the case.\(^{65}\) The Tribunal made three observations in
this regard: First, it noted that certain international arbitration decisions have awarded
compound interest.\(^{66}\) Second, it held that previous decisions have acknowledged the
*possibility* of awarding compound interest.\(^{67}\) Third, it cited opinions in academic literature
according to which compound interest must be awarded as “damages” in order to fully
compensate the expropriated owner and not to let the state unjustly enrich itself.\(^{68}\)

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\(^{62}\) *CDSE v. Costa Rica*, supra note 1, at 94.

\(^{63}\) *Id.*, at 96.

\(^{64}\) *Id.*, at 97.

\(^{65}\) *Id.*

\(^{66}\) *Id.*, at 98. The Tribunal *inter alia* refers to *Kuwait v. Aminoil* (66 International Law Reports 518, 613 (1982)).

\(^{67}\) *Id.*, at 99 (refering to the *Norwegian Shipowners’ Claims* (UN Reports of International Arbitral Awards, vol.
1, 307, at 341 (1922))).

\(^{68}\) *Id.*, at 101 – 102.
In the present case of Santa Elena, the panel considered the long period of twenty-two years (1978 – 2000), in which CDSE has been unable to use its property in any way while bearing the burden of maintaining the property, sufficient to award compound interest. Based on the applicable interest rate, the Tribunal determined $11.85 million in interest was payable to CDSE. This amount seems staggering in comparison to the actual compensation of only $4.15 million. Whilst the Tribunal cited a few instances where international arbitration tribunals reached the same conclusion, it failed to explain why the long waiting period alone was sufficient to require compound interest to be paid. Moreover, as Brower and Wong rightly argue, the Tribunal did not offer any numerical analysis as to how it arrived at this figure and awarded an amount that was not in line with the “generally prevailing rates”. However, other authors argue that compound interests only reflect modern economic practices. In contrast to simple interest, where a certain fixed percentage of the compensation is paid, compound interest takes into account the loss of the use of money. If the appropriate compensation was paid instantly, it could have been invested in alternative assets, such as shares or debt instruments. Thus, the investors would have been entitled to interest on a year-on-year, where interest is also paid on interest and not just on the principal.

3. Environmental Protection and International Investment Law

Notwithstanding the remaining controversy around compound interest in international law, the Santa Elena arbitration became especially famous for shaping the relationship between environmental protection and international investment law. Due to the absence of a bilateral agreement between Costa Rica and the U.S., the arbitration serves as a leading case for all sorts of expropriatory environmental measures on the international plane. The objective of this Section is to give an overview of how the ruling was received in academic circles and how it relates to other – similar – arbitral awards.

69 Id, at 105.
70 Brower/Wong, supra note 3, at 22.
3.1. Criticism in Academic Literature

The main criticism raised in response to the arbitral decision revolved around the priority it appeared to give to investment protection over the rules of environmental protection. As Sands\(^{72}\) rightly argues, the Tribunal faced a dilemma. If domestic (and international) rules of environmental protection were to prevail over investment protection, international investor protection would be prone to abuse by states.\(^{73}\) Conversely, if the Tribunal’s view was right then the practical consequence may be to prevent States from protecting their environment in accordance with their domestic and international obligations.\(^{74}\) To address this disparity, Sands argues that a more balanced approach ought to be adopted to integrate environmental concerns into the norms of foreign investment protection.\(^{75}\) In Fauchald’s\(^{76}\) opinion, the Santa Elena case places the economic burden of environmental measures solely on public authorities, as they have to offer full compensation when the state adopts expropriatory environmental policies. Hence, poor countries in particular may become reluctant to safeguard their environment in order to avoid expensive compensation claims and protracted arbitration. This stands in stark contrast to the international goals of environmental protection as reflected by Goal 13 to 15 of the 2015 Sustainable Development Goals (SDGs).\(^{77}\)

Beharry and Kuritzky\(^{78}\) argue that the Tribunal took a narrow approach with respect to the state’s police powers. They argue that the arbitral system allows for too much discretion on the part of the Tribunal and that treaties as well as arbitral panels need to take into account factors such as the legitimacy of the State’s aim, the nature of the measure and the due

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73 Id.
74 Id.
75 Id, at 10.
process in order to better consider environmental harm in their decisions. 79 Vadi criticises the arbitrators for their heavy focus on the “sole-effect doctrine” in the Santa Elena dispute. According to this principle (in contrast to the “police-power doctrine”) the effect of property deprivation (and therefore the impact on the economic value of the investment) is exclusively relevant for determining the amount of the damages. The expropriation’s public purpose has no impact whatsoever on mitigating or eliminating the compensation due. 81 This becomes clear when looking at the Tribunal’s statement that “expropriatory environmental measures are similar to other expropriatory measures and the obligation to compensation remains”. 82 According to Perry-Kessaris however, the criticism of the sole-effect doctrine in the Santa Elena case is misplaced as the expropriation was of direct nature. This aligns with Kriebaum’s view, who notes that the sole-effect doctrine is used to determine whether an indirect expropriation has occurred by assessing the (economic) effect of the governmental measure on the investment. When a certain level of interference with property rights is exceeded, full compensation becomes due regardless of what public interest is at stake. 85 This would endorse the Tribunal’s view that environmental considerations must not play a role in calculating the compensation due.

De lege lata the Tribunal’s decision to reject environmental considerations appears to align with its discretionary powers under the relevant rules of international investment law. Nevertheless, there are voices in literature that favour a more nuanced approach to bridge the tensions between environmental protection and investor protection. As mentioned above, Fauchald considers the “police-power doctrine” more adequate as it requires the burden to either be shared between the public authorities and the investor, or be placed entirely on the investor. 86 This could in turn mean that environmental considerations may constitute a basis

79 Id, at 429.
81 Id.
82 See CDSE v. Costa Rica, supra note 1, at 45.
85 Id.
86 Fauchald, supra note 78, at 25.
for reducing the compensation. Against the backdrop of existing case law however, a general rule to distribute the economic effects of environmental protection is non-existent. Awarding the value of the actual investment made by the investor, rather than the loss of potential future profits, is undoubtedly one step in the right direction and has for instance been adopted in the Pyramids case.\footnote{See below 3.2.} In Santa Elena, the Tribunal was more conservative as it based the value of an approximation between the investor’s claim and the compensation offered by Costa Rica. Interestingly, even Costa Rica’s appraisal (on which the compensation of $1.9 million was based) assigns a special commercial value to the property.\footnote{Compare CDSE v. Costa Rica, supra note 1, at 86 (noting that the} If real burden-sharing was to be applied, the investor would only be entitled to the actual investment made, which was approximately $400,000 plus interest – less than a tenth of what CDSE demanded in the course of the dispute.

True and fair burden-sharing however, would have to be integrated by way of contractual arrangements (i.e. BITs). ICSID tribunals would likely overstep their powers if they were to introduce such rules by the means of quasi-judicial discretion. Whilst a few BITs already promote sustainable development in theory, Fauchald notes that de lege ferenda efforts to integrate environmental concerns are often reactive, lack a much-needed long-term strategy and create bilateral instead of multilateral frameworks.\footnote{Id, at 46-47.}

### 3.2. Other Seminal Arbitration Decisions on Environmental Protection

As the Santa Elena case did not thoroughly elaborate on the issue of environmental protection in international investment law, it makes sense to look at other – similar – arbitral awards. In the Metalclad\footnote{Metalclad Corporation v. The United Mexican States, ICSID Case No. ARB(AF)/97/1, (30 Aug. 2000).} case for instance, an ICSID arbitration panel had to decide whether a U.S. company was entitled to compensation after Mexican authorities had prohibited its operations of a hazardous waste landfill.\footnote{Id, at 30.} These measures were taken after local residents had complained about developing aggressive diseases and water pollution for years.\footnote{Id, at 30.} The key question was whether or not Metalclad was entitled to damages under Article 1105 of the NAFTA, a provision reminiscent of the rules under international law on
investor expropriation. The Tribunal concluded that the Mexican government was obliged to compensate Metalclad for its investment in the project.\textsuperscript{93} The Tribunal did not pick up Mexico’s argument that the public purpose of protecting the environment as well as the state’s citizens has an impact on the compensation to be paid. Rather it explained in great detail how an operating permit could amount to an expropriation.\textsuperscript{94} Asteriti considers the Metalclad case the clearest articulation of the above-mentioned “sole-effect doctrine”, as it focused on the effect of the measure on the investor’s property rather than elaborating on the public purpose.\textsuperscript{95} However, unlike the Santa Elena case, the Metalclad Tribunal did not compensate the foreign investors for potential future profits arguing that such approach would be wholly speculative.\textsuperscript{96} While the Tribunal in Santa Elena did not compensate all potential future profits, it awarded a multiple of the amount invested by CDSE to acquire the land.

The Pyramids case\textsuperscript{97} is another leading case worth noting in this context. The decision revolved around the question of cultural heritage protection under international investment law and seems to offer a more balanced approach. Essentially, the Claimant (Southern Pacific Properties Limited) submitted to the ICSID Tribunal that Egypt had violated its agreements to allow the development of two international tourist resorts at the Pyramids Oasis as well as the Mediterranean coast.\textsuperscript{98} Egypt in fact cancelled the project after antiquities were discovered in the area. The site later (after the investment was made) became part of the UNESCO World Heritage, just like the Guancaste province in the Santa Elena case. In determining the fair and equitable amount of compensation due, the Tribunal stressed that Egypt’s international obligation to protect such sites would have rendered the Claimant’s activities unlawful. This had strong implications for the compensation due as the Tribunal

\textsuperscript{93} Id., at 34.
\textsuperscript{94} Id., at 107.
\textsuperscript{96} Id., at 121.
\textsuperscript{97} Southern Pacific Properties (Middle East) Limited v. Arab Republic of Egypt, ICSID Case No.ARB/84/3 (20 May 1993).
could only award *lucrum cessans* until 1979, the date when the site was declared a World Heritage site.\(^99\)

Again this view deviates from the Tribunal’s assessment in the *Santa Elena* case. By applying methods of approximation the Tribunal at least partially awarded *lucrum cessans* to CDSE. In contrast to the *Pyramids* case, the *Santa Elena* decision argues that the approximation would take into account the “potential for tourism development”.\(^100\) Thus, the Tribunal ignored the fact that the property was added to the UNESCO World Heritage List, ignoring the constraints this puts on a large-scale tourism project as envisaged by CDSE.

### 4. Conclusion

The *Santa Elena* decision highlights both the merits of settling an enduring legal battle by means of international arbitration, and the inherent difficulty of rendering a fair and equitable judgement in the absence of appropriate evidence and documentation. Whilst the Tribunal gave an excellent overview of the international rules relating to expropriation cases in the international field, it faced a formidable challenge in assessing the property’s true value in 1978. However, in contrast to other international arbitral awards the Tribunal paid little attention to the question of whether environmental obligations (e.g. imposed by the World Heritage status) affect the amount of compensation due. Admittedly, the lack of reasonable evidence with respect to *Santa Elena’s* value in 1978 left little choice but to resort to the inaccurate method of approximation. It can be hoped that future arbitration cases concentrate more on the intricate relationship between investment and environmental law and better explain how these opposing legal regimes interact with one another. Moreover, BITs ought to play a vital role in establishing a balanced framework of burden sharing between countries and foreign investors in order to achieve sustainable development and align economic interests with efforts to preserve the global ecological system.

\(^99\) *SPP v. Egypt*, at 190.

\(^100\) *CDSE v. Costa Rica*, *supra* note 1, at 94.