Case summary

Compañía del Desarrollo de Santa Elena, S.A.

v

The Republic of Costa Rica

Year of the award: 2000
Forum: ICSID
Applicable law: Domestic law of Costa Rica and international law

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<td>Mr. L. Yves Fortier, President</td>
<td>2 June 1995 – request for arbitration</td>
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<td>Professor Sir Elihu Lauterpacht</td>
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I. Executive Summary

CDSE, a company established in Costa Rica by US nationals, purchased in 1970 for tourism development the property known as “Santa Elena”, consisting over 30 kilometres of Pacific coastline. In 1978, Costa Rica issued a decree ordering expropriation of this property from CDSE, in order to use Santa Elena for environmental purposes, and proposed to pay CDSE US$ 1,900,000 in compensation.

CDSE disagreed with the offered amount (under its own assessment done also in 1978, the value of the property was US$ 6,400,000). The subsequent court proceedings before Costa Rican national courts that dragged for 20 years did not lead to any definite result. In 1995, under the political pressure from the US, Costa Rica agreed to submit the dispute to ICSID arbitration. In the arbitral proceedings CDSE claimed US$ 40,000,000 including the current value of the property and interest.

The task before the arbitral tribunal was to determine the amount of compensation to be paid to CDSE by Costa Rica (the fact of expropriation as such was not in dispute). The Tribunal first determined the date on which the valuation had to be made. Despite the fact that after the 1978 Decree, CDSE remained in possession of the property, the Tribunal decided that the property was expropriated in 1978, as CDSE was deprived of the opportunity to make economic use of the property. It did not agree with the Claimant that it should be paid the current value of Santa Elena.

The Tribunal then determined the value of the property in 1978 – by performing an “approximation” of two alternative assessments carried out in 1978 by parties. In doing so, the Tribunal took into account the circumstances of the case that it considered relevant, in particular – property’s potential for tourism development. The Tribunal arrived at the figure of US$ 4,150,000 (without any explanation as to how this figure was calculated but the exact midpoint between the two competing evaluations).

The Tribunal also discussed the issue of simple/compound interest in international jurisprudence and decided that in cases of property takings, award of compound interest was fair, if warranted by the circumstances of a particular case. The Tribunal thus awarded US$ 11,850,000 interest.

II. Factual Background and Claims of the Investor

Compañía del Desarrollo de Santa Elena, S.A. (“CDSE”) is a Costa Rican corporation, the majority of whose shareholders are US nationals. In 1970 it purchased the property known as “Santa Elena”. This property is located in Costa Rica and consists of over 30 kilometres of Pacific coastline, as well as numerous rivers, springs, valleys, forests and mountains. CDSE acquired Santa Elena for US$395,000 with the intention of developing it as a tourist resort and residential community. CDSE proceeded to design a land development program and undertook various financial and technical analyses of the property with a view to its development.
In 1978 Costa Rica issued an expropriation decree for Santa Elena (the “1978 Decree”), in order to add this territory to the Santa Rosa National Park and thus contribute to the preservation of rare species. Although the property remained in the de facto possession of CDSE, the latter could no longer pursue its tourism-development project. To compensate for expropriation, Costa Rica proposed to pay CDSE the sum of approximately US$ 1,900,000.

CDSE did not object to expropriation as such but contested the price fixed by Costa Rica. CDSE made its own expert evaluation of the property (also in 1978) and claimed US$ 6,400,000 as compensation. During the subsequent twenty-year period the parties were involved in litigation before Costa Rican courts, with the amount of compensation remaining unresolved. Under political pressure from the US Government, in 1995 Costa Rica consented to turn this matter to ICSID arbitration.

The central purpose of the arbitration was to determine the value of the expropriated property and, accordingly, the amount of compensation that had to be paid to CDSE by Costa Rica. CDSE claimed approx. US$ 40,000,00 representing, according to its estimates, the current fair market value of the property and interest. Costa Rica maintained that the value of the property should be determined as of the date of the expropriation (1978) and insisted on the figure of US$ 1,900,000.

III. Findings on Merits

The Tribunal did not need to make findings on merits because both parties agreed that expropriation of property had taken place. The issue was only to determine the appropriate amount of compensation.

IV. Findings on Damages

A. Applicable Law

The dispute was not based on any investment treaty. Due to the absence of the agreement between the parties as to the applicable law, the Tribunal had to apply “the law of the Contracting State party to the dispute […] and such rules of international law as may be applicable.” (Article 42(1) of the ICSID Convention)

The Tribunal established that Costa Rican laws relating to the appraisal and valuation of expropriated property were generally consistent with the accepted principles of public international law on the same subject (the Tribunal did not name these principles). The Tribunal ruled that to the extent that there may be any inconsistency between the two bodies of law, the rules of public international law must prevail. (para.64) Thus, international law was “controlling” in the dispute.¹

¹ In particular, the Tribunal applied the rule of international law that the value of expropriated property has to be determined as on the date of expropriation, and not at the time of compensation, as provided in Costa Rican law.


**B. Standard of Compensation**

In determining the standard of compensation, the Tribunal did not refer to any legal provision. It stated simply that it was common ground between the parties that the compensation should be based upon the “fair market value” of the property. The Tribunal further specified that the fair market value is “what a willing buyer would pay to a willing seller” (para.73) and that it should be calculated by reference to “highest and best use” of the property (para.70).

**C. Valuation**

In terms of valuation, the Tribunal addressed two issues: (1) the date, on which the market value was to be assessed, and (2) determination the fair market value itself.

1. **Date, on which the market value was to be assessed**

   The Claimant argued that the fair market value of Santa Elena was equivalent to its present day value. The Respondent objected to this and stated that the relevant date for valuation purposes was the date of the expropriation decree (1978).

   The Tribunal started on the premise that the date of expropriation was the relevant date for evaluation. Basing itself on existing international jurisprudence, the Tribunal stated that “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 economic use of his property”. (para.77) Accordingly, the “expropriated property is to be evaluated as of the date on which the governmental ‘interference’ has deprived the owner of his rights or has made those rights practically useless.” (para.78)

   In the present case, the Tribunal determined that despite the fact that CSDE remained in possession of Santa Elena also subsequently to the 1978 Decree, the taking of property still occurred in 1978. This is because after the 1978 Decree, CDSE irretrievably lost the practical and economic use of the property. (paras. 80-81).

2. **Determination of the fair market value**

   As mentioned above, in 1978 both parties made their respective assessments of the property. Costa Rican assessment equaled US$ 1,900,000 while CDSE’s estimate amounted to US$ 6,400,000. The Tribunal had no other evidence of what the property was actually worth at the date of expropriation.

   In a situation when the Tribunal could not go back in time to make an evaluation of property, it decided, with reference to several other international arbitrations, that it had to make an “approximation” based on the two appraisals effected by the parties in 1978 (thus, the Tribunal’s figure had to be somewhere in-between the two extremes), while exercising its own judgment and taking into account all relevant circumstances.
of the case. Particularly, in this case the Tribunal found relevant the fact that at the
time of expropriation the property had a potential for tourism development.
(paras.89-94)

Without any further explanation of how it came to its conclusion, the Tribunal
determined that a sum of US $4,150,000 constituted a reasonable and fair
approximation of the value of the property at the date of its taking. The Tribunal did
not make a breakdown into the heads of damages compensated (e.g. capital value, lost
profits etc.). Neither did it give its assessment, in monetary terms, of factors that it
took into account. The awarded compensation represented the exact midpoint between
the two competing evaluations.

D. Interest

At length, the Tribunal discussed the question of a possibility to award compound, as
opposed to simple, interest. The Tribunal noted the tendency in international legal
proceedings to award simple interest but stated that this tendency principally applied
to cases of injury or simple breach of contract. According to the Tribunal, the same
considerations did not apply in cases of valuation of property or property rights,
where award of the compound interest was not excluded where warranted by the
circumstances of the case. (para.97)

As a result of its review of international jurisprudence and academic writings, the
Tribunal concluded that no uniform rule of law has emerged as regards the
determination of whether compound or simple interest was appropriate in any given
case. Rather, the determination of interest was a product of the exercise of judgment,
taking into account all of the circumstances of the case at hand and especially
considerations of fairness. (para.103)

Applying this postulate to the situations concerning takings of property when the
former owner did not receive due compensation in time, the Tribunal stated that “the
amount of compensation should reflect, at least in part, the additional sum that
[owner’s] money would have earned, had it, and the income generated by it, been
reinvested each year at generally prevailing rates of interest.” (para.104) The Tribunal
did not indicate how to determine the “generally prevailing rates of interest”.

The Tribunal determined that it would be fair to award compound interest in the case
at hand on the basis of the following: “CDSE is entitled to the full present value of the
compensation that it should have received at the time of the taking. Conversely, the
taking state is not entitled unjustly to enrich itself by reason of the fact that the
payment of compensation has been long delayed.” (par.101) At the same time, the
Tribunal decided not to award full compound interest because CDSE, while not being
able to use the property for tourism development, remained in possession of the
property and was able to exploit it to a limited extent. (para.105)

Without specifying the applied interest rate or setting out its calculation (in particular,
the adjustment of compound interest to make it less than “full”), the Tribunal stated
simply that the compensation and interest together equaled US$ 16,000,000 (thus the
interest for the period of more than 20 years amounted to US$ 11,850,000).
According to one estimate, the award was mathematically equivalent of applying a simple interest rate of 13.13% or a compound interest rate of 6.40%.

E. Legal Costs

Again, without any explanation, the Tribunal ruled that each party should bear the expenses incurred by it in connection with the arbitration, and that the costs of the proceedings should be borne by the parties in equal shares.

V. Implications / Initial Analysis

- **The value of the case** is diminished because the Tribunal did not describe how it came to the amount of awarded compensation. However, it elucidated some principles on the award of damages (e.g., what is “fair market value” and at which point in time it should be determined), as well as the principles concerning simple/compound interest.

- To correctly determine the market value of the expropriated property, it is important to determine the **date of expropriation**. This is the date on which the governmental “interference” has deprived the owner of his rights or has made those rights economically useless.

- International law requires determining the value of the expropriated property on the **date of expropriation**, as opposed to the date of award/compensation. In this case, the more than 20-year delay in providing due compensation did not result in altering this approach. More recent case law (in particular *ADC v Hungary*) suggest that in case of unlawful expropriation, a tribunal may award the value of investment if it has increased during the time leading up to the arbitral award.

- The **“approximation” approach** of the Tribunal effectively amounted to “splitting the baby”, account being taken of the circumstances considered relevant.

- The Tribunal addressed, in a substantial detail, the issue of **simple v compound interest** and came to the conclusion that in expropriation cases (concerned with valuation of property), award of compound interest is fair from an economic point of view, unless circumstances of a particular case lead to a contrary conclusion.

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