

# Kluwer Arbitration Blog

## Alejandro Díaz Gaspar v. Costa Rica: FET in the Spotlight

Karima Sauma (CICA-AmCham) · Wednesday, August 17th, 2022

On 29 June 2022, an ICSID Tribunal composed of Alexis Mourre, Luis González García and Adolfo Jiménez issued its [Final Award](#) in the case brought by Alejandro Diego Díaz Gaspar, a Spanish national, against Costa Rica. The majority of the Tribunal ultimately found minor breaches of the underlying [Costa Rica-Spain Bilateral Investment Treaty](#) (the “Treaty”) but declined to award any damages to Claimant.

This is the most recent ICSID award rendered against Costa Rica. In the author’s view, this decision confirms its place as a country respectful of international law and the obligations acquired with respect to foreign investors. In total, Costa Rica has been Respondent in thirteen ICSID cases, only two of which are currently pending. Most of these cases stem from specific, individual situations that relate to different types of investments, industries and measures. The country’s experience with ISDS has been overwhelmingly positive, including two cases (*David Aven* and *Cervin Investissements*) in which the tribunals ruled in favor of the state and even awarded Costa Rica its costs.

This post will address the origins of the dispute between Alejandro Diego Díaz Gaspar and Costa Rica, the applicable legal framework, the questioned governmental measures, the Tribunal’s approach to the fair and equitable treatment standard (“FET”) standard and finally the Tribunal’s decision.

### **Background to the dispute**

This particular case arose out of a growing conflict between Ibérico (the company incorporated by Mr. Díaz Gaspar in Costa Rica through which he purchased a poultry processing plant), and the neighbors of the area where the plant was located, due to supposed bad odors and other health concerns.

When Ibérico took over the plant, it increased the facility’s production capacity without obtaining the pertinent authorizations (such as the environmental assessment). The repeated complaints from the neighbors triggered several inspections from the Costa Rican sanitary authorities.

On 27 January 2016, the health authorities issued a sanitary order noting that Ibérico had not obtained the required authorization to expand the capacity of the plant’s wastewater treatment system (“STAR”). The order gave the company a two-month cure period. However, two days later,

this order was replaced by another one, which instead allowed for a one-day compliance period.

On 12 February 2016, the health authorities ordered the technical closure of the STAR, to be complied with by 19 February 2016. Additionally, another resolution dated 15 February 2016 suspended the veterinary operation certificate (“CVO”) and all plant activities effective 19 February 2016.

On 19 February 2016, an administrative court issued an interim measure in favor of Ibérico, halting the closure of the STAR and the CVO suspension. Despite this, the plant still suspended its activities between 19 February and 23 February 2016. The plant later reopened, but eventually ceased its operations. The cause of the shutdown of the plant was a disputed fact in the arbitration.

Claimant filed its claim in 2019 before ICSID alleging:

- Expropriation of Claimant’s investment.
- Breach of the obligation to promote and create favorable conditions for Claimant’s investment.
- Breach of the obligation to grant a fair and equitable treatment.
- Obstruction of the investment through arbitrary and discriminatory measures.
- Breach of the national treatment obligation.

Claimant sought at least US\$ 81 million in damages, plus US\$ 1 million in moral damages.

### **The Applicable Legal Framework to the Investment and Governmental Measures**

The Tribunal first determined that Respondent’s legal framework offered the Government certain leeway in the exercise of its supervisory duties.

Claimant questioned the following governmental measures:

- Irregular inspections in January 2016.
- Sanitary orders, reports and decisions detecting nonexistent disconformities and granting impossible deadlines to comply, which lead to disproportionate administrative acts.
- The resolution that suspended the CVO.
- The technical closure of the STAR and the plant.

The Tribunal found that the inspections were normal, especially for this type of industry. Regarding the sanitary orders, the Tribunal extensively analyzed and concluded that Respondent had not offered a compelling reason for why it had replaced the two-month cure period. As for the suspension of the CVO, the Tribunal found one irregularity; however, it was deemed irrelevant because the resolutions in question were suspended through the decision of the administrative court.

In view of the Tribunal’s finding regarding the sanitary order that granted the one-day period, it also concluded that the decision to close the STAR was premature and irregular. The order in question was deemed to be excessive and lacking legal reasoning.

### **The Protection and Admission Standard**

The Tribunal determined that the Treaty should be interpreted as having two parts: one related to obligations applicable to the admission phase of the investment (which are regulated in Article II), and the other concerning the treatment obligations owed to admitted investments. This led the Tribunal to conclude that the State acts at issue, which took place *after* the investment was admitted, could not constitute a breach of Article II-1.

### **Fair and Equitable Treatment**

The core of this case revolved around the FET standard. The Tribunal first analyzed the Treaty's FET provision and noted that Article III-1's wording clearly provided that the Parties did not agree to an FET obligation beyond that provided in international law. Thus, Article III-1 reflected the minimum standard of treatment under customary international law.

On that basis, the Tribunal determined that a state act that is arbitrary, notoriously unjust, unlawful, idiosyncratic or discriminatory, as well as lacking in transparency or a serious breach of administrative due process, is contrary to the minimum standard of treatment under customary international law, and must be examined on a case – by – case basis.

For the Tribunal, two circumstances must be considered: that the dispute was based on a treaty that promotes and protects investments, and that the disputed measures referred to the Government's exercise of regulatory powers.

When analyzing Claimant's argument related to the violation of legitimate expectations, the Tribunal emphasized that the legitimate expectations that are relevant to an FET breach are those generated at the moment when the investment is made, not in the course of its operation.

The Tribunal determined that since Claimant did not prove that it had carried out a proper due diligence on the regulatory framework at the moment of making the investment, and it had not received specific commitments on the part of the State, it could not have had any legitimate expectations relating to the evolution of the legal framework. Based on this, the Tribunal concluded that Claimant did not prove that it had legitimate expectations that could be relevant towards a breach of the FET standard.

Further, in analyzing the FET standard, the Tribunal explained that the breach must be considered with respect to the State's legal system as a whole, meaning that if there is an error and the State promptly corrects it, the measure cannot give rise to State responsibility under international law.

The Tribunal considered that the unexplained modification of the two-month cure period constituted a breach of Costa Rica's duties to hold a reasonable and transparent administrative process. The Tribunal also suggested that the two-month period would have been reasonable, considering that the authorities knew of the plant's irregularities since 2015, and that it would have allowed Ibérico to regularize its situation.

In response to these measures, Ibérico obtained a favorable interim measure that suspended the sanitary orders and received notification on 19 February 2015. However, the plant remained closed for the three following days. In consequence, the Tribunal considered that this closure was not attributable to the State, since the sanitary orders had been effectively suspended.

In addition, the Tribunal concluded that Ibérico's financial distress could not be attributed to the Government's acts and had begun since at least in November 2015.

Claimant also argued that public officials had created a defamation campaign against Ibérico; however, the Tribunal concluded that there was no proof that the statements made interfered with Claimant's rights.

Finally, the Tribunal also dismissed Claimant's request for moral damages based on its finding that the decisions ordering the closure of the Plant do not constitute treaty breaches because they were promptly corrected by the administrative court.

### **No Violation of Other Standards**

The Tribunal noted that the prohibition of arbitrary measures contained in Article III-2 also forms part of the FET standard under Article III-1. The Tribunal decided that the sanitary closure, the CVO suspension orders, as well as few of the Health Minister's statements to the press were arbitrary; however, these were promptly corrected by Costa Rica's Judiciary. These conclusions also applied to breaches of Article II-1 as well as Article III-2.

As for the expropriation claims, the Tribunal ultimately rejected them, citing that for an indirect expropriation to exist, one of the necessary elements is that the deprivation of the use and enjoyment of the investment must be caused by acts attributable to the State. In this case, the Claimant voluntarily closed the plant (since the irregular sanitary orders were promptly remedied by the local courts); therefore, the closure could not be attributed to the State.

### **Decision**

In sum, the majority of the Tribunal concluded that:

- By substituting the sanitary orders, closing the STAR, suspending the CVO and closing the plant for three days, the Government of Costa Rica acted arbitrarily and inconsistently with its FET obligations.
- However, these breaches were promptly corrected by the the administrative court.
- The fact that Ibérico later went on to shut down its plant for three additional days could not be attributable to the State.
- Since Costa Rica corrected the arbitrary measures, these could not constitute a breach of the State's international obligations under the Treaty.
- The Minister of Health's statements to the press constituted a breach of the FET standard, but Claimant did not prove that these statements caused any damages.

In his partial dissenting opinion, Mr. González agreed with the majority's finding that the case should be dismissed in its entirety; however, he disagreed with the majority's reasoning on the assessment of FET and submitted that the Tribunal majority had applied a much lower standard when identifying two instances of arbitrariness.

## Conclusion

Even though the Tribunal did not award damages to Claimant, the Tribunal's FET analysis merits attention because of the standard applied, especially regarding the Minister of Health's statements to the press. The decision also serves as a strong reminder of the importance of having sound public policies that are backed by a system of checks and balances. The Tribunal eventually sided with Costa Rica because it was able to prove that the Judiciary corrected the "arbitrary measures" carried out by the Executive Branch that resulted in a breach of the Treaty's FET standard. This speaks to the State's ability to correct certain conducts to avoid being in breach of international law.

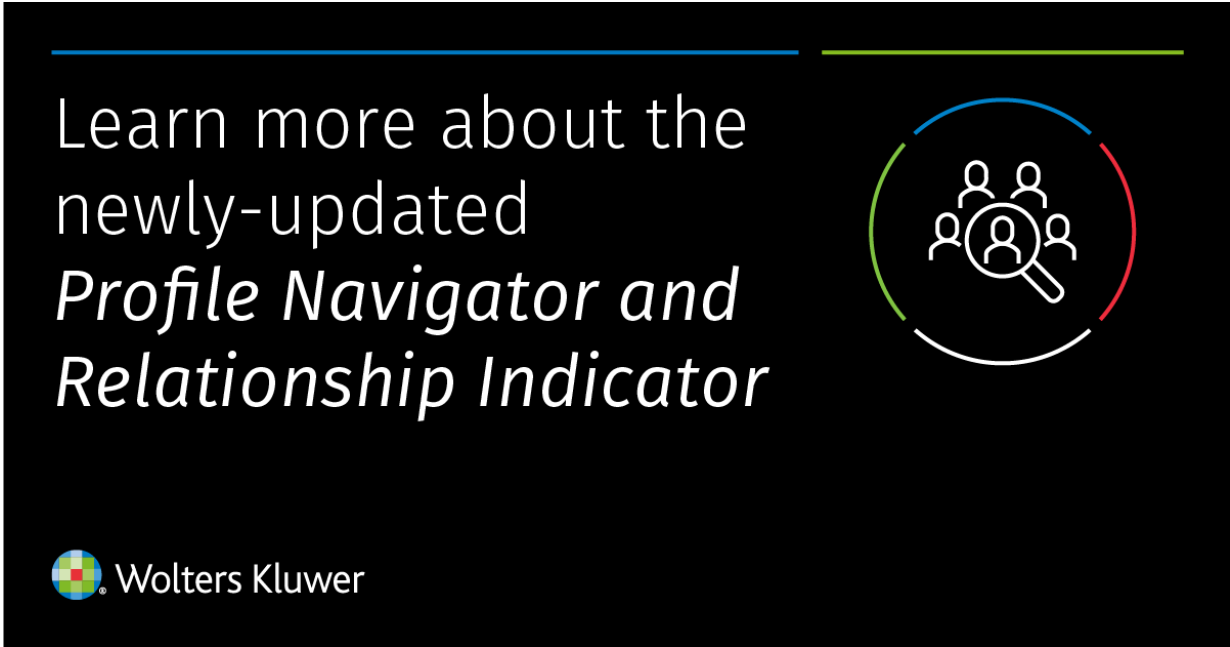
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