CLAIMS FOR REFLECTIVE LOSS UNDER INVESTMENT TREATIES

David Gaukrodger

Senior Legal Adviser
Investment Division
OECD

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Outline

1. Contrast between domestic law and unique ISDS interpretation generally allowing reflective loss claims
2. Allowing reflective loss claims expands scope of ISDS and generates multiple potential claims for the same injury
3. Treaty shopping and forum shopping in ISDS using attribution of reflective loss claims
4. Minority shareholder claims for reflective loss
5. Effects of availability of reflective loss claims for some shareholders on corporate law and finance
6. Company recovery regimes: NAFTA-style derivative action and deemed foreign company models
7. Links and contact
Domestic Law: “No Reflective Loss” principle bars shareholder claims for reflective loss
ISDS: Reflective Loss Claim

**Government**

**GRETEL**
Indirect covered shareholder (100%)

**CHELSEA**
Foreign covered shareholder (60%)

**DONNA**
Domestic and foreign non-covered shareholders (20%)

**FRANK**
Foreign covered shareholder (20%)

**ABLE**
Domestic operating company

**BAKER**
Creditors of ABLE

**HANSEL?**

**JERRY?**

- Alleged harm
- ISDS claim
ISDS: Multiple Reflective Loss Claims – Unrelated Entities

- **GreteL**: Indirect covered shareholder
- **Chelsea**: Foreign covered shareholder
- **Donna**: Domestic and foreign non-covered shareholders
- **Frank**: Foreign covered shareholder
- **Hansel?**
- **Jerry?**
- **Able**: Domestic operating company
- **Baker**: Creditors of Able

Graphical representation:

- ISDS claim from Government to GreteL
- Alleged harm from Donna to Able
- ISDS claim from Able to Baker

Entities involved:
- Domestic and foreign non-covered shareholders
- Domestic operating company
- Creditors of Able
- Indirect covered shareholder
- Foreign covered shareholder
- Foreign covered shareholder

Questions:
- Hansel?
- Jerry?
ISDS: Multiple Reflective Loss Claims – Related Entities

- **Government**
  - **ISDS claim**
  - **alleged harm**
  - **ABLE**
    - Domestic operating company
  - **GRETEL**
    - Indirect covered shareholder
  - **CHELSEA**
    - Foreign covered shareholder
  - **DONNA**
    - Domestic and foreign non-covered shareholders
  - **FRANK**
    - Foreign covered shareholder
  - **HANSEL?**
  - **JERRY?**
  - **BAKER**
    - Creditors of ABLE
ISDS: Potential Claims 1

- Government
  - ISDS claim
  - alleged harm
- GreteL
  - Indirect covered shareholder (100%)
- Chelsea
  - Foreign covered shareholder (60%)
- Donna
  - Domestic and foreign non-covered shareholders (20%)
- Frank
  - Foreign covered shareholder (20%)
- Hansel?
- Jerry?
- Able
  - Domestic operating company
- Baker
  - Creditors of Able
ISDS: Potential Claims 2

ISDS claim

Government → ISDS claim → GRETEL (Indirect covered shareholder, 100%)

alleged harm

Government → alleged harm → ABLE (Domestic operating company)

Claim under contract or domestic law

ABLE → creditors → BAKER (Creditors of ABLE)

DONNA (Domestic and foreign non-covered shareholders, 20%)

FRANK (Foreign covered shareholder, 20%)

CHELSEA (Foreign covered shareholder, 60%)

HANSEL?

JERRY?
**ISDS: Potential Claims 3**

- **DONNA**: Domestic and foreign non-covered shareholders (20%)
- **Government**: Alleged harm
- **CHELSEA**: Foreign covered shareholder (60%)
- **ABLE**: Domestic operating company
- **GRETEL**: Indirect covered shareholder (100%)
- **DONNA**: Domestic and foreign non-covered shareholders (20%)
- **Frank**: Foreign covered shareholder (20%)
- **BAKER**: Creditors of ABLE
- **HANSEL?**
- **JERRY?**

**ISDS claim**

**ISDS claim**
ISDS: Treaty Shopping Using Attribution of Reflective Loss Claim(s)

KAPPA has several choices for shopping

Government

Claim 1
Claim 2
Claim 3
Claim 4

KAPPA
100% - covered
Nationality: K
K-G Treaty

EPSILON
80% - covered
Nationality: E
E-G Treaty

DELTA
100% - covered
Nationality: D
D-G Treaty

ALPHA
Operating company

Non-covered Shareholders
20%

Creditors

Creditors

alleged harm
KAPPA has several choices for shopping

Claim 1

Claim 2

Claim 3

Claim 4

KAPPA
100% - covered
K-G Treaty
ICSID

Epsilon
80% - covered
E-G Treaty
PCA

Non-covered Shareholders
20%

Delphi
100% - covered
D-G Treaty
AI-SCC

Creditors

Alpha
Operating company

Creditors
ISDS: Minority Shareholder in Large Domestic Company

- Domestic non-covered shareholders (91%)
- Covered financial investor, e.g. hedge fund (9%)
- Large domestic company; Eg. market capitalisation USD 100 billion
- Government
  - alleged harm
- Creditors
  - ISDS claim
- Government
  - alleged harm
- Creditors
  - ISDS claim

[Graph showing the relationships and claims]
Domestic Law: “No Reflective Loss” principle bars shareholder claims for reflective loss
Corporate finance: repayment rank order

- Secured debt
- Unsecured debt
- Subordinated debt
- Preference shares
- Ordinary shares (common equity)

Domestic Law: Who is Protected? – All Investors

- Indirect Shareholder
- Indirect shareholder
- Indirect shareholder

No Reflective loss claims by shareholders

- Direct Shareholder Entity
- Operating company
- Creditors

- Government

alleged harm

claim

sole permissible claimant
ISDS Reflective Loss Claim: **Who is Protected?**

* Note: This slide and the next slide have been corrected from the versions discussed at the side meeting. Frank’s treaty coverage, which was inadvertently omitted, has been restored. Frank is not protected by the claim by Chelsea. It may bring its own ISDS claim if its individual loss is significant; this would generate multiple claims for the government and high costs while still leaving investors unprotected. Only a company claim protects all investors. On the categories of excluded and potential claimants for reflective loss in ISDS and claim incentives, see Gaukrodger (2013b), pp. 47-48, [http://dx.doi.org/10.1787/5k3w9t44mt0v-en](http://dx.doi.org/10.1787/5k3w9t44mt0v-en).
ISDS Reflective Loss Claim: **Who is not Protected?**

- **Government**
  - **ISDS claim**
  - **alleged harm**
    - **ABLE**
      - Domestic operating company
    - **GRETEL**
      - Indirect covered shareholder
    - **CHELSEA**
      - Foreign covered shareholder
    - **DONNA**
      - Domestic and foreign non-covered shareholders
    - **FRANK**
      - Foreign covered shareholder
    - **HANSEL?**
    - **JERRY?**
    - **BAKER**
      - Creditors of ABLE
ISDS: NAFTA-style Derivative Claim

1. alleged harm

2. derivative ISDS claim on behalf of ABLE; requires waiver of other recourse by CHELSEA and ABLE

3. if claim successful, damages payable only to ABLE (company)

GRETELF
Indirect covered shareholder (100%)

CHelseAF
Foreign covered shareholder (60%)

DONNA
Domestic and foreign non-covered shareholders (20%)

FRANK
Foreign covered shareholder (20%)

ABLE
Domestic operating company

Government

Baker
Creditors of ABLE

HANSEL?

Jerry?
ISDS: Deemed Foreign Company Claim

1. alleged harm
2. ISDS claim
3. if claim successful, damages payable only to ABLE (company)


For questions or comments regarding this presentation, please contact david.gaukrodger@oecd.org.