CLAIMS FOR REFLECTIVE LOSS UNDER INVESTMENT TREATIES

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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

Indirect Shareholder

Indirect Shareholder

Indirect Shareholder

Direct Shareholder Entity

No Reflective loss claims by shareholders

Government

Operating company

Creditors

alleged harm

sole permissible claimant

claim
ISDS: Reflective Loss Claim

- **Government**
  - **ISDS claim**
  - **Alleged harm**
  - **ABLE**
    - Domestic operating company
  - **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?**
  - **BAKER**
    - Creditors of ABLE

- Alleged harm:
  - Government to ABLE
  - GRETEL to DONNA
  - CHELSEA to ABLE
  - DONNA to ABLE
  - FRANK to ABLE

- ISDS: Reflective Loss Claim
ISDS: Multiple Reflective Loss Claims – Unrelated Entities

Government

ISDS claim

alleged harm

ABLE
Domestic operating company

ISDS claim

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

Domestic and foreign non-covered shareholders

Foreign covered shareholder

Indirect covered shareholder
ISDS: Multiple Reflective Loss Claims – Related Entities
ISDS: Potential Claims 1

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

ISDS claim

alleged harm
ISDS: Potential Claims 2

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

CHELSEA
Foreign covered shareholder (60%)

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

ABLE
Domestic operating company

HANSEL?

FRANK
Foreign covered shareholder (20%)

BAKER
Creditors of ABLE

Claim under contract or domestic law

alleged harm

Creditors of ABLE
ISDS: Potential Claims 3

- **DONNA**: Domestic and foreign non-covered shareholders (20%)
- **Domestic operating company**
- **CHELSEA**: Foreign covered shareholder (60%)
- **GRETEL**: Indirect covered shareholder (100%)
- **DONNA**: Domestic and foreign non-covered shareholders (20%)
- **FRANK**: Foreign covered shareholder (20%)
- **HANSEL?**
- **JERRY?**
- **ISDS claim**

Alleged harm from Government to **ABLE**: Domestic operating company

Creditors of **ABLE**

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

KAPPA has several choices for shopping

Claim 1

Claim 2

Claim 3

Claim 4

alleged harm

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

Government
ISDS: Forum Shopping Using Attribution of Reflective Loss Claim(s)

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

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

Alpa
Operating company

Non-covered Shareholders
20%

Creditors

Creditors

Alleged harm

Government
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
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

- Government
- Operating company
- Creditors

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?**

- **DONNA**: Domestic and foreign non-covered shareholders
- **CHELSEA**: Foreign covered shareholder
- **GRETEL**: Indirect covered shareholder
- **ABLE**: Domestic operating company
- **HANSEL?**
- **JERRY?**
- **FRANK**: Foreign covered shareholder
- **BAKER**: Creditors of ABLE

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**ISDS claim**

**alleged harm**
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)
ISDS: Deemed Foreign Company Claim

1. alleged harm

2. ISDS claim

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


Contact

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