Shareholder Claims for Reflective Loss in Investment State Dispute Settlement: A “Component-by-Component” Approach to Reform Proposals

Informal Discussion Paper

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1. Introduction

1. This paper provides preliminary material for initial discussion of model treaty text and policies to govern individual shareholder claims for reflective loss and related issues in treaty-based claims in ISDS.\(^1\) It follows UNCITRAL Working Group III expressions of interest in the issues, an UNCITRAL Secretariat note\(^2\), and an Academic Forum paper.\(^3\) It also builds on earlier work and inter-governmental discussions at the OECD on shareholder claims for reflective loss in ISDS as well as other work.\(^4\) The issues were explained and discussed at a joint UNCITRAL Secretariat-OECD-Academic Forum webinar for Working Group III delegates in July 2020.\(^5\)

2. The UNCITRAL Secretariat note observes that the availability of shareholder claims for reflective loss in ISDS is closely linked with several concerns identified by the Working Group that deserve reforms.\(^6\) These include concerns related to claims for reflective loss include the increased number of cases and multiple proceedings in ISDS; the cost and duration of ISDS proceedings; the lack of consistent outcomes and interpretations; and double recovery, possibly leading to excessive damages. The note also pointed out

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\(^1\) This paper has been prepared by the OECD Secretariat. Contact: david.gaukrodger@oecd.org. Comments on a draft from Dr. Felix Steffek, Associate Professor, Faculty of Law, University of Cambridge are gratefully acknowledged. The views expressed herein are those of the author and do not necessarily reflect the views of the OECD or of governments that participate in OECD-hosted dialogue on international investment policy. It cannot be construed as prejudging ongoing or future negotiations or disputes arising under investment treaties. This document and any map included herein are without prejudice to the status of or sovereignty over any territory, to the delimitation of international frontiers and boundaries and to the name of any territory, city or area.


\(^3\) See Julian Arato, Kathleen Claussen, Jaemin Lee & Giovanni Zarra, Reforming Shareholders Claims in ISDS (2019).


\(^6\) As noted in the UNCITRAL Secretariat note, shareholders incur “reflective loss” through an injury to “their” company. An injury to a company typically leads to a loss in the value of shares in the company. It is a reflective loss because it is due to the company injury. The concept is addressed further below.
that permitting reflective loss claims can distort corporate law and finance. It took note that these elements relating to shareholder claims for reflective loss could contribute to undermine the predictability and legal certainty for States, investors and shareholders alike, potentially leading to increases in cost of ISDS. It also noted that they may in particular have a negative impact on the predictability of the ISDS system from the respondent State’s perspective, as it is difficult to assess whether there would be any additional claims and who the claimants might be.

3. Governments at the OECD noted a range of similar issues following earlier inter-governmental consideration of shareholder claims for reflective loss in ISDS, as set out in a summary of the discussion:

The Chair noted that many policy reasons for the bar on reflective loss had been identified in Professor Ferran’s presentation, the background papers and the discussion. In no particular order, these included the risk of inconsistent decisions, exposure to double recovery, the impact on predictability, hindering settlement, facilitating treaty shopping, and upsetting the hierarchy of claims so that a claimant gets better treatment than under normal legal principles. The Chair suggested that these policy issues raised by shareholder claims for reflective loss all seem to also be relevant to ISDS. Indeed, many of the issues raised by shareholder claims, such as inconsistencies, treaty shopping and double recovery, are frequently at the core of government discussions about ISDS generally.  

4. The discussions at the OECD did not identify any policy reason that would explain the general allowance of shareholder claims for reflective loss in ISDS, or the difference between a government’s domestic law and its treaty policies on the issue. It was noted that the “lack of an identifiable policy rationale for existing law was an important finding and merited further attention”. The UNCITRAL Secretariat paper on reflective loss notes these preliminary findings.

5. This paper turns to the practical work of developing draft model provisions in this area. As governments have noted in Working Group discussions, discussions over model language can provide a useful basis for discussion. It can help clarify concepts and assist with policy decisions and negotiations.

6. The work addresses standing for treaty-based ISDS. Shareholder claims under shareholder-government contracts are excluded. Such contracts can be an avenue open to shareholders and governments. However, the discussion below focuses on claims under treaties.

7. To facilitate work, the paper envisages developing separate components that can be addressed sequentially. The discussion of complex issues can benefit from focus on separate potential elements. The discussion can encompass more elements over time. Potential components can be discussed as part of larger regimes with the impact better understood. Alternative components can be compared. All of the proposed provisions are without prejudice to government policy decisions. The use of components can help governments to determine whether they agree on common approaches.

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8 Id., p. 19.


10 For clarity, repeated references to each particular draft model rule applying only where desired by governments have been eliminated – the qualification applies generally. Similarly, reference to rules only being rules for possible adoption are omitted.
8. The paper briefly set out below the rationale for priority attention to developing first a component composed of model rules generally aligned with domestic law on shareholder standing to bring claims for reflective loss. A second area for priority attention is a component composed of rules to allow certain domestic companies to bring claims in ISDS based on the characteristics of company shareholders or other factors. The sequential development of alternative and additional components is foreseen.

9. The draft rules address shareholders and companies. References to the “company” refer to the company in which the shareholder owns shares and generally to the “operating company” that is active in the real economy and that incurs alleged direct loss due to government action.

10. Shareholder claims for reflective loss refer to claims by shareholders on their own behalf seeking remedies for themselves. As discussed further below, claims by shareholders on behalf of the company for remedies for the company are not claims for reflective loss – they are derivative claims for the company’s direct loss.

11. The balance of the paper is organised as follows. Section 2 provides background. It first outlines the unique nature of the current ISDS interpretation generally allowing claims for reflective loss, in contrast to all other legal systems. It then describes the rationale and approach for developing components in sequence.

12. Section 3 (at pp. 17-18 below) sets out model text for the first component: a draft rule that a shareholder generally only has standing to bring claims for its direct loss, together with definitions, clarifications and exceptions. Section 4 provides commentary on the draft rule. Section 5 briefly identifies a few additional issues for consideration.
2. Background

2.1. The unique nature of the current general interpretation in ISDS

13. Shareholders in companies can be harmed in two broadly different ways. First, they can suffer direct loss that is unrelated to loss suffered by the company in which they hold shares. For example, denial of the right to attend and vote at general meetings of shareholders affects the shareholder directly. Its loss is not derived from a company loss. Such injury is relatively rare and shareholder recovery for it is uncontroversial. Second, shareholders (and others) can suffer reflective loss as a result of an injury to the company: the market value of shares in the company or its dividend distributions may fall. This occurs routinely whenever a company is injured. Company creditors can also suffer reflective loss when injury to the company reduces its assets available to repay the debt.

14. OECD analysis and inter-governmental discussions have demonstrated that domestic corporate law and other bodies of law apply what has been called a general “no reflective loss” principle to shareholder claims. Following analysis of both common law (United States; Canada; United Kingdom; Australia; Hong Kong (China)) and civil law (Germany; France) systems, the findings were confirmed in discussions at an OECD-hosted inter-governmental Roundtable:

The Roundtable recognised that all of the advanced national law systems surveyed to date, including both leading common law and civil law systems, generally bar shareholder claims for reflective loss due notably to concerns about consistency raised by such claims. Some participants from countries with legal systems not surveyed in the background paper confirmed that their national law also generally bars shareholder claims for reflective loss. Additional government input in this area was encouraged, but there was a consensus about the widely-applied prohibition under domestic law. The general no reflective loss principle is also applied in customary international law and under the European Convention on Human Rights.\(^\text{11}\)

Shareholder recovery of reflective loss is generally barred because the company owns the claim for its direct loss.

15. An interpretation frequently applied in ISDS takes a different approach. In ISDS, treaty-covered shareholders of the company have generally been allowed to recover directly for reflective losses they incur as a result of injury to the company. Numerous ISDS tribunals have allowed direct or indirect shareholders to claim for and recover reflective loss for themselves. The company is no longer the sole owner of the claim as under domestic law. The general rule in ISDS is the opposite of the general rule under domestic law.

16. Under the interpretation, treaty-covered shareholders are in the enviable position of having the best of both worlds: limited liability for debts incurred in the corporate name and direct compensation for

losses resulting from corporate losses due to government action found to be in violation of the treaty. This “cushy position” for covered shareholders is unique to ISDS.12

17. The differences between the interpretation of many treaties and national corporate law are accentuated by two characteristics of ISDS cases: (i) the acceptance of reflective loss claims by indirect shareholders higher up the corporate chain; and (ii) the wide variety of covered direct and indirect shareholders allowed to recover reflective loss, including 100% parent companies, majority shareholders and minority shareholders.

18. As noted in the OECD discussions, the ISDS interpretation is also unique in comparison with other international law. Customary international law is much less developed than national law with regard to corporate law and shareholder claims. There is no equivalent in international law to the detailed statutes governing corporations under national law. However, the principles with regard to shareholder claims for reflective loss have been squarely addressed by the International Court of Justice in two cases. The general principle that shareholder reflective loss cannot form the basis of a claim under general international law is well-established.13 Like national courts, the European Court of Human Rights also generally bars shareholder claims for reflective loss.14 The Court noted that if claims were not restricted to the company, it would be hard to determine which shareholder or creditor constituencies should be allowed to bring claims against governments.

19. A range of senior courts have recently reaffirmed the general rule barring shareholder claims including in cases involving government regulation. The Grand Chamber of the European Court of Human Rights reaffirmed the general rule in 2021 in rejecting shareholder standing to challenge banking regulation under the European Convention on Human Rights.15 In *Starr Int’l Co. Inc. v. United States*, a US federal appellate court applied the rule in 2017 in rejecting a shareholder claim against the United States for reflective loss in a case involving US Federal Reserve Board action toward AIG in the context of the 2008 financial crisis; leave to appeal was denied by the US Supreme Court.16 The Grand Chamber of the Court

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12 See, e.g., *Kagan v. Edison Bros. Stores Inc.*, 907 F.2d 690, 693 (7th Cir. 1990) (“The [shareholder and company creditor] investors are asking us to disregard [the company’s] corporate form.... Although the [shareholder] plaintiffs want us to allow them to recover for injuries mediated through [the company], they most assuredly do not want us to hold them liable for [the company’s] debts. They seek the best of both worlds: limited liability for debts incurred in the corporate name, and direct compensation for its losses. That cushy position is not one the law affords.”); *Alford v. Frontier Enterprises, Inc.*, 599 F.2d 483 (1st. Cir. 1979) (same); see generally Gaukrodger, D., *Investment Treaties as Corporate Law: Shareholder Claims and Issues of Consistency*, OECD Working Paper on Investment 2013/3, pp. 15-23 (surveying advanced corporate law systems; shareholders of companies generally benefit from limited liability but cannot claim for reflective loss).


14 See, e.g., *Agrotexim v. Greece*, (Eur. Ct. H.R. 1995) §§ 68-71; *Géniteau v. France (no. 2)*, Case 4069/02 (Eur. Ct. H.R. 2005) (finding shareholder claim for reflective loss inadmissible; “La Cour rappelle sa jurisprudence, selon laquelle il n’est justifié de lever le « voile social » ou de faire abstraction de la personnalité juridique d’une société que dans des circonstances exceptionnelles …”) [The Court recalls its case law, according to which it is only justified to ‘pierce the corporate veil’ or to ignore the juridical personality of a company in exceptional circumstances …] (author translation)

15 See *Albert and Others v. Hungary*, European Court of Human Rights (Grand Chamber) (7 July 2020).

16 *Starr Int’l Co. Inc. v. United States*, 856 F.3d 953 (Fed. Cir. 2017) (“We conclude that Starr and the shareholders represented by Starr lack standing to pursue the equity-acquisition claims directly, as those claims
of Justice of the European Union (CJEU) rejected a shareholder claim against the European Central Bank arising out of the termination of a banking licence in 2019; only the directly affected bank could claim.\footnote{European Central Bank v. Trasta Komercbanka (Joined Cases C-663/17 P, C-665/17 P and C-669/17 P) (2019).} Government entities successfully opposed shareholder standing in all these cases. In a private law context, the UK Supreme Court reaffirmed the rule in 2020 in \textit{Marex}, underlining that it has been applied in many Commonwealth jurisdictions (Australia, the Cayman Islands, Hong Kong (China), Ireland, Jersey and Singapore), albeit with some differences in reasoning, as well as in the UK.\footnote{Sevilleja v. Marex Financial Ltd, [2020] UKSC 31; see id., para. 78 (citing Commonwealth cases).} The Supreme Court of Canada reaffirmed the rule for both civil law cases and common law cases in 2018 and dismissed a shareholder claim at a preliminary stage.\footnote{See \textit{Brunette v. Legault Joly Thiffault, s.e.n.c.r.l.,} 2018 SCC 55 (official English translation; French original available at same webpage); id., para. 24 (“In certain cases, the civil law produces a conclusion similar to that which would arise under the common law. This is one such case. As this Court has noted, there is often ‘a striking similarity between the civil law and the common law approaches.’”) (citation omitted).}

20. As many courts have noted, a shareholder chooses to invest in shares of a company. It is a choice that entails well-defined consequences. For example, in \textit{Marex}, Lord Reed quoted an earlier case:

\begin{quote}
When the shareholder acquires a share he accepts the fact that the value of his investment follows the fortunes of the company and that he can only exercise his influence over the fortunes of the company by the exercise of his voting rights in a general meeting.\footnote{Marex, para. 35 (Lord Reed), quoting \textit{Prudential}, p. 224; id. Paras 99, 108 (Lord Hodge).}
\end{quote}

As recognised by the court in \textit{Agrotexim}, different shareholders and other corporate constituencies frequently have frequently different views about how the corporation should act.\footnote{See, e.g., \textit{Agrotexim v. Greece,} (Eur. Ct. H.R. 1995) § 65 (“It is a perfectly normal occurrence in the life of a limited company for there to be differences of opinion among its shareholders or between its shareholders and its board of directors as to the reality of an infringement of the right to the peaceful enjoyment of the company's possessions or concerning the most appropriate way of reacting to such an infringement.”) See David Gaukrodger, \textit{Claims for Reflective Loss under Investment Treaties} (2020) (“Gaukrodger Presentation”), available at \url{https://unctitral.un.org/sites/unctitral.un.org/files/media-documents/unctitral/en/gaukrodger_english.pdf}; French version at \url{https://unctitral.un.org/sites/unctitral.un.org/files/media-documents/unctitral/fr/programme-fr.pdf}.}


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described in a presentation during the Joint Webinar.\textsuperscript{23} Certain diagrams are also incorporated into the UNCTTRAL Secretariat paper on claims for reflective loss.\textsuperscript{24}

22. The interpretation allowing claims for reflective loss expands the number of potential claims and claims in ISDS. It is widely recognised that the acceptance of shareholder claims for reflective loss favours the interests of claimant shareholders, but can harm the interests of other investors – the other shareholders and company creditors. It may be more in the nature of a “pro-claimant” interpretation than a “pro-investor” interpretation.

23. Claimants and their beneficial owners\textsuperscript{25} have not hesitated to take advantage of the unique ISDS interpretation. As a recent statistical study underlines, “investing indirectly through conduit subsidiaries, and filing ISDS [claims] through them, are mainstream rather than niche corporate strategies” in ISDS. Such claims reportedly account for a fourth to a third of ISDS cases filed each year.\textsuperscript{26} The interpretation generates substantial revenues for the arbitration community (counsel, arbitrators, experts, arbitration institutions).\textsuperscript{27} In addition to revenues from cases, pre-dispute negotiations and settlements can generate additional revenues. The general application of normal corporate law principles could reduce such revenues.

2.2. Proceeding component by component – rationale and approach

24. As set out above, the paper begins to develop separate draft components that can be addressed sequentially in order to facilitate discussion. Potential components can then be discussed as part of larger regimes with the impact better understood. Different components can be compared once they have been specified. The discussion can encompass more elements over time. Basic components can be adjusted.

25. A first component establishes the normal corporate law rule, as applied in domestic law and general international law, generally requiring that an individual shareholder demonstrate direct loss in order to have standing to bring a claim. The rule generally bars shareholder claims for reflective loss. It includes exceptions.

\textsuperscript{23} Joint Webinar on Reflective Loss (minutes 13-29), available at https://www.youtube.com/watch?v=EcMPWdZns3A&feature=youtu.be.


\textsuperscript{25} Beneficial owners refer generally to beneficial owners of shareholders. Where reflective loss claims are permitted including for indirect shareholders, beneficial owners of shareholders can attribute reflective loss claims to their preferred controlled shareholder entity. Beneficial owners can create additional corporate entities as indirect shareholders. Such entities can be claimants in ISDS if claims for reflective loss are permitted. See Gaukrodger Presentation, slide 10 (ISDS: Treaty Shopping Using Attribution of Reflective Loss Claim(s)), available at https://unctital.un.org/sites/unctital.un.org/files/media-documents/unctital/en/gaukrodger_english.pdf; Joint Webinar on Reflective Loss (minutes 28-29), available at https://www.youtube.com/watch?v=EcMPWdZns3A&feature=youtu.be.


\textsuperscript{27} A number of governments have expressed interest in information about the economic aspects and incentives in ISDS as part of their consideration of policies. See, e.g., OECD, Government perspectives on investor-state dispute settlement: a progress report (2012), p. 16 (“because investment law itself is based on expectations about the power of economic incentives to affect behaviour … the possible impact of economic incentives on arbitrators should be considered”)
26. A second component would create additional recourse to remedies in ISDS for directly-injured domestic companies rather than shareholders.

27. A third component would seek to restate expressly current ISDS interpretations generally accepting shareholder standing to claim reflective loss. It would also consider emerging theories on possible limits on a few claims. The fourth component would seek to develop effective new procedural fixes to address concerns with the broad availability of shareholder claims for reflective loss and the various types of multiple claims. This would include issues such as possibly modifying the scope for consolidation, res judicata or other claim preclusion.

28. The first component merits priority attention for several reasons. First, it appears that there is significant government “demand” for a treaty rule clarifying or providing that direct loss is required and reflective loss claims are excluded. A range of governments (including Argentina; Canada; Gabon;)

29. Transparent provisions setting out the interpretation, rather than leaving the issue to brief treatment in lengthy opinions in arbitration cases, would provide valuable information transparently to the market. This is particularly important where an interpretation differs from well-established general rules on corporate law, governance and finance. At present, SMEs and others may be unaware of the ISDS interpretation.

30. A restatement of the arbitral interpretation would facilitate consideration of issues that it generates, help to evaluate and define as appropriate theories emerging in arbitration, and allow consideration of the appropriate institutions for resolution of the issues that need to be decided under the interpretation.

31. Preliminary analysis at the OECD suggests that it will be challenging to develop effective rules in these areas if shareholder claims for reflective loss are permitted, in part due to the scope for treaty and forum shopping generated by the acceptance of them. See David Gaukrodger, Investment Treaties and Shareholder Claims: Analysis of Treaty Practice (OECD Working Papers on International Investment 2014/03), pp. 34-43, available at https://doi.org/10.1787/5jxvk6shpvs4-en. Development of model rules in this area will allow evaluation of the new issues that would need to be resolved in reflective loss cases under modified procedural approaches and the potential litigation costs to resolve them. See, e.g., Gabriel Bottini, Admissibility of Shareholder Claims under Investment Treaties (2020), pp. 71-74 (setting out three pages of questions that tribunals should consider in resolving whether a claim for reflective loss is admissible under a flexible approach to allowing reflective loss claims); Alicia Grace v. Mexico, Non-disputing Party Submission of the Government of Canada Pursuant to NAFTA Article 1128 (24 Aug. 2021), paras. 20 (noting that, at the damages phase, the GAMI tribunal “cautioned that awarding damages for reflective loss would produce insurmountable difficulties with respect to quantification of any loss to a particular investor”) (citing GAMI, Final award paras. 116-121).

32. See, e.g., Webuild S.p.A. (formerly Salini Impregilo S.p.A.) v. Argentine Republic, Decision on Jurisdiction and Admissibility, (23 Feb. 2018), para. 174 (reporting that Argentina interpreted the treaty as barring shareholder standing for a claim in relation to the contractual rights of the company); BG Plc v Argentina, Award, (24 Dec. 2007), para. 191 (reporting on Argentina interpretation that treaty did not grant jurisdiction over shareholder claims for damage to the value of its shares caused by or derived from measures adopted by Argentina which had a negative impact on the activities of a company in which it held shares).


34. See Kontinental Conseil Ingénierie v. Gabonese Republic, PCA Case No. 2015-25, Award, 23 December 2016 (para. 192) (reporting on Gabonese interpretation that shareholder had no standing (qualité pour agir) under the treaty because only the company signed the contracts and there was no cession of rights).
Guatemala; India; Jordan; Republic of Korea; Morocco; Mexico; Peru; Syria; and the United States have interpreted treaties as excluding shareholder claims for reflective loss. However, they have rarely been successful in having their interpretations adopted in ISDS arbitral decisions. The issue

34 See Kappes v. Republic of Guatemala, Respondent’s Preliminary Objections under Article 10.20.5 of CAFTA-DR (16 Aug. 2019), paras. 6, 45 (“[Shareholder] Claimants’ standing is limited to claims for losses arising out of direct injury to their shareholding rights. Because Claimants are seeking to recover damages arising out of purported injuries to [the company’s] rights, Claimants’ claims are inadmissible and should be dismissed.”)

35 See, e.g., Louis Dreyfus Armateurs SAS (France) v. Republic of India, Award (11 Sept. 2018), para. 275 (reporting on Indian interpretation that a shareholder has no standing because the treaty “does not permit investors to bring so-called ‘reflective loss’ claims – i.e., claims for harm to the value of their shares in companies allegedly mistreated, without any alleged mistreatment of the investors’ shareholder rights as such”; reflective loss claims by indirect shareholders are also impermissible).

36 See Fouad Alghanim & Sons Co. for General Trading & Contracting, W.L.L. and Fouad Mohammed Thunyan Alghanim v. Hashemite Kingdom of Jordan, Award, 14 December 2017 (para. 118) (reporting on Jordanian interpretation that “the alleged mistreatment on which the [shareholder] Claimants rely related only to the rights of UTT [the company], not the Claimants, and the Claimants cannot sue for harm done to a separate corporation”; “Claimants fail to establish any breach of the BIT that specifically relates to the Claimants’ 35% interest in UTT”).

37 See Republic of Korea v. Davami [2019] EWHC 3580 (Comm) para. 70 (reporting on Korean interpretation that claimant shareholders lacked standing for claim in ISDS in respect of the loss caused by interference with what, if they were property or assets at all, were property or assets of the company in which they owned shares)]

38 See Carlyle Group LP v. Kingdom of Morocco, Respondent’s Reply on Jurisdiction and Admissibility (7 Sept. 2020), p. 123 (“The loss and damage identified by the Claimants was incurred indirectly through the Cayman entities and cannot form the basis of a valid claim under FTA Article 10.15.1(a)”)

39 See, e.g., Alicia Grace v. Mexico, Escrito de Contestación de Demanda (1 June 2020), p. 164 (“Las Demandantes con supuestas participaciones minoritarias directas carecen de legitimación para presentar reclamaciones según el Artículo 1116 por pérdidas reflejas (‘reflective losses’)”) [The Claimants who allegedly hold direct minority shareholdings do not have standing to claim under Article 1116 for reflective losses] (author translation); GAMi v. Mexico, Escrito de Contestación de Mexico, §§ 166-67, pp. 61-64 (24 Nov. 2003). For NAFTA generally, see Meg N. Kinneer et al., Investment Disputes under NAFTA, An Annotated Guide to NAFTA Chapter 11 (2006 & 2008 Supp.), pp. 1116-6 - 1116-7 (Under NAFTA Parties’ interpretation, so-called “derivative damages” – damages based on the diminution in value of the interest in the enterprise owned by the investor – are not compensable under Article 1116).


41 See Guris v. Syria, Award (31 Aug. 2020), para. 169 (reporting on Syrian interpretation that “a shareholder’s harm from measures/acts directed (primarily or exclusively) at the company is harm actionable only by the company, not the shareholder”); see Investment Arbitration Reporter, “Syrian award (and dissent) at heart of recent set-aside decision has finally surfaced” (20 May 2021) (reporting on award and providing link to it), available at https://www.iareporter.com/articles/syrian-award-and-dissent-at-heart-of-recent-set-aside-decision-has-finally-surfed/ (paywall).

42 See, e.g., GAMi v. Mexico, Submission of the United States (non-disputing party) (30 June 2003); Carlyle Group LP v Morocco, Submission of the United States of America (non-disputing party submission) (4 Dec. 2020).

43 Discussion herein will focus in particular on the views of governments with publicly-available submissions. Arbitration awards generally report only in summary form on government views on the issue; there can be ambiguity at times about the government interpretations which can at times be framed in different ways.
continues to require repeated government and claimant briefing including recently. Arguments and interpretations on the issue can be lengthy, but are rarely directly available.  

29. Second, rules in this area are generally found in court cases rather than legislation. There are few examples of domestic statutes. The absence of examples of statutory language can present a challenge for treaty drafting. Multilateral work can prepare effective explicit treaty rules or interpretations where arbitral outcomes have deviated from desired outcomes. The model draws on a variety of sources including comparative domestic law and international law and analysis. The provisions have been developed for possible use in treaties or other materials and do not seek to state customary international law.

30. Third, model rules in the first component would allow interested governments to ensure better alignment of ISDS with general corporate law and general international law. Leaving the issues to courts in domestic law on the one hand and to arbitrators in ISDS on the other has generated contradictory outcomes – a general bar on claims under case law in domestic law and general acceptance in ISDS. Some governments may wish to provide investor protection while continuing generally to apply orthodox corporate law principles with regard to reflective loss claims, principles that are widely seen conducive to major investments by the full range of investors in companies, to successful companies, and to efficient dispute settlement. At this stage, express language developed after due analysis, consideration and discussion may be the most effective path to this result.

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44 For example, in the on-going Carlyle Group LP v Morocco case, the claimants submitted 11 single spaced pages of argument on the reflective loss issue in 2020 solely in response to the non-disputing party submission of the United States setting out its long-held view that shareholder reflective loss claims are barred under all its treaties since the 1994 NAFTA. See Carlyle Group LP v Morocco, Claimants’ Response to the Submission of the United States of America under Article 10.19.2 (22 Dec. 2020), pp. 2-12; id., Submission of the United States of America (non-disputing party submission) (4 Dec. 2020). As noted, only a small number of submissions in ISDS are publicly available.

45 See, e.g., Clayton v. Canada, Canada’s Counter-Memorial on Damages, paras. 22-25 (explaining that exclusion of claims for reflective loss achieves important policy goals):

“Allowing investor claims for reflective loss can strip assets from the company to the detriment of creditors and non-claimant shareholders. … Introducing different priority rankings over corporate assets unsettles the predictability of the corporate form as a structure for investment … [T]he risks of double recovery and inconsistent decisions arise, and concerns for judicial economy grow, as the number of cases brought to address the same harm increases. … [L]ike separate legal personality, delegated management is a core characteristic of the corporation. The corporation’s directors and officers make most business decisions, including whether to commence or settle litigation. They have a fiduciary duty to act in the corporation’s best interests, by considering diverse corporate constituents including minority shareholders. The directors and officers may not consider commencing or continuing arbitration against the host state to be in the corporation’s long-term interest. If shareholders can claim autonomously for reflective loss under Article 1116, they can disregard such concerns. Moreover, the respondent government may see little value in settling with the company when new shareholders might raise claims over the same events. … It would be inappropriate for a shareholder to take advantage of the separate legal status of a corporation to shield itself from potential liability, but then disregard that legal status for the purpose of making claims for reflective loss.” (citations omitted).
31. Fourth, as illustrated for example by recent decisions of the Colombian and French constitutional courts, recent views expressed by the European Parliament and earlier and recent decisions by the US Congress, an increasing range of governments have constitutional, legal or policy constraints that mandate that their investment treaties do not provide preferential rights for covered investors over domestic investors. The Parties to CETA agreed on a joint interpretation that “CETA will not result in foreign investors being treated more favourably than domestic investors.” There is growing interest in ensuring a level playing field and increasing requests for clarity about the comparative rights of each group in practice. Claims for reflective loss for covered shareholders in ISDS, and the resulting capacity to access corporate assets to the detriment of company creditors, are not available to domestic shareholders of the same company. It is a notable example of a treaty interpretation under which covered shareholders have preferential rights.

46 See Constitutional Court of Colombia, Judgment No. C-252/19, 6 June 2019 (finding that joint government interpretations of the Colombia-France BIT to ensure that it does not provide greater rights to covered investors than to Colombian investors would be necessary before ratification); Constitutional Court of Colombia, Judgment No. C-254/19, 6 June 2019 (similar findings on the Colombia-Israel FTA). See also summaries of the cases in Constitutional Court of Colombia, Communication No. 19 of 2019, 5-6 June 2019. All materials are in Spanish. The case is briefly summarised in IA Reporter (2019), “Colombia round-up: Newly approved bilateral investment treaties, dispute settlement discussions, pleadings and decisions in ongoing arbitrations”, 8 July 2019.

47 See, e.g., European Parliament resolution of 8 July 2015 containing the European Parliament’s recommendations to the European Commission on the negotiations for the Transatlantic Trade and Investment Partnership (TTIP) (2014/2228(INI)) (addressing recommendation to the European Commission to ensure that foreign investors benefit “from no greater rights than domestic investors”).

48 The US Congress in the Trade Act of 2002 (art. 2102(a)(3)) mandated as a negotiating objective to “ensur[e] that foreign investors in the United States are not accorded greater substantive rights with respect to investment protections than United States investors in the United States.” A 2007 agreement between the US Congress and President Bush reaffirmed this objective. See United States Trade Representative, Bipartisan Trade Deal (May 2007) (describing bipartisan agreement in trade policy including on continuation of no greater rights provision from the 2002 legislation and recognition of it by the USTR as a principal negotiating objective). The most recent US trade promotion authority legislation in 2015 contained a similar objective. See Pub. Law 114–26 (29 June 2015), art. 102(b)(4).

49 Joint Interpretative Instrument on the Comprehensive Economic and Trade Agreement (CETA) between Canada and the European Union and its Member States (2016), art. 6(a).

50 Standing rules in ISDS do not address the scope of substantive rules. While some investment treaties have carefully defined provisions, in other treaties key provisions are set out in vague terms and are frequently subject to inconsistent interpretations. See Note by the UNCITRAL Secretariat, Possible reform of investor-State dispute settlement (ISDS): Consistency and related matters A/CN.9/WG.III/WP.150 (28 Aug. 2018), paras. 4-18 (citing cases and identifying a range of inconsistent interpretations). Governments that may consider that the standing rules extend beyond the substantive scope of the treaty can contest claims on the merits. Conversely, governments that may consider that substantive rights extend beyond the scope of standing in the rule may be able to bring state-to-state claims. Many investment treaties provide for binding state-to-state dispute settlement (SSDS) over claims relating to the “application or interpretation” of the treaty. The provisions generally co-exist with ISDS provisions. A range of governments have chosen to apply only SSDS to all or most investment protection claims in a number of recent
32. The preferential rights could be addressed through changes to domestic law to allow shareholder claims for reflective loss and shareholder access to corporate assets. However, it does not appear that any government is considering a change to its corporate law generally to allow shareholder claims for reflective loss against the government, companies or others. Nor does it appear that any multinational enterprise or business organisation supports change generally in the law to allow shareholder recovery of reflective loss against companies and governments. The recent court cases cited above make it clear that the general rule is well established in domestic and regional law. The availability of clear model treaty provisions aligned with well-established domestic law may thus be of value and importance to treaty policy for governments and parliaments in a range of economies. It may help them to explain relative treatment to interested stakeholders such as domestic companies interested in attracting domestic share capital, domestic shareholders or workers.

33. As noted, the second component, which will be addressed in future work, will address company remedy regimes: remedies in ISDS for certain directly-injured domestic companies. A single company claim by the injured company is the normal regime in corporate law. There is no shareholder access to remedies against the party injuring the company. Concurrent claims arising from the same injury by companies and shareholders, or by multiple shareholders, are consequently rare. Litigation costs are lowered.

34. A directly-injured company will generally have recourse under domestic law or in commercial arbitration or both. However, if the company is incorporated in the host state (or otherwise has host state nationality), it will normally not have access to ISDS.

35. Company remedy regimes can provide additional remedies in ISDS for specified companies. They can address perceived concerns about potential recourse in domestic law or commercial arbitration. In contrast to the first component, for which there are few examples of express statutory or treaty language, a substantial number of investment treaties contain express provisions for company recovery.51 The basic principle in most existing regimes is that a domestic company controlled by a foreign covered shareholder can obtain access to remedies in ISDS. In recent multilateral treaties, this has generally taken the form of a type of derivative action: the controlling shareholder is empowered to bring a claim on behalf of the company.

36. Company remedy regimes differ fundamentally from shareholder claims for reflective loss. First, the remedy goes to the company, not only to certain shareholders. A remedy for a company automatically benefits all investors and stakeholders in the company. This includes covered shareholders, domestic shareholders and creditors. In reflective loss claims, only the claimant shareholder loss is addressed. Remedies payable to shareholders can be detrimental to the company, non-claimant shareholders and company creditors.

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51 For examples in multilateral treaties, see, e.g., Additional Protocol to the Pacific Alliance, CPTPP, USMCA, CETA.
37. Second, in a company remedy regime, the full injury can be addressed in a single claim.\textsuperscript{52} Multiple claims are rare. In contrast, allowing shareholder claims for reflective loss claims makes multiple claims available, and makes multiple claims necessary to repair the injury. Tactical procedural behaviour by beneficial owners of shareholders can further increase the number of claims.

38. It is valuable to consider the first two components together. For example, governments that have been leading proponents of including derivative action mechanisms in their treaties to allow for company remedies have generally categorically opposed reflective loss claims under their treaties without identifying any exceptions. They interpret their treaties as barring reflective loss claims while creating a regime for company recovery under certain conditions. They have described the two elements as interrelated policy decisions.\textsuperscript{53}

39. While the two components are related, they are distinct. Governments can choose policies on each independently. They can decide whether or not generally to limit shareholder claims to direct loss. In either case, they can decide whether or not to include a company recovery regime and how to design its criteria for access.

40. The development of a single compromise solution in this area may be challenging. The component-by-component approach can develop different regimes with predictable consequences. It can help clarify concepts. It can facilitate analysis and help governments to negotiate including over possible broadly agreed approaches.

\textsuperscript{52} Company remedy regimes involve claims for the company’s direct loss. The claim is based on and seeks a remedy for the company’s direct loss. Company remedy regimes are not claims for reflective loss as framed herein. A remedy for the company will benefit shareholders, including the claimant shareholder but also all others, and creditors. Their reflective losses may be reduced or eliminated. But the claim is for the company’s direct loss.

\textsuperscript{53} The regimes are described here principally as set forth by relevant governments that make their interpretations public including in non-disputing party submissions. Arbitral interpretations have differed in some cases. Model clauses can help ensure government intent is achieved.
3. Draft model text for a first component: a shareholder generally only has standing in ISDS to bring claims for its Direct Loss

**Article XX. Standing for shareholders.**

1. A covered shareholder claiming on its own behalf shall only have standing to claim for Direct Loss. It must demonstrate Direct Loss in addition to the existence of an applicable treaty obligation.

2. For a claim to be for Direct Loss,

   The covered shareholder’s loss must be incurred in its capacity as a shareholder. The covered shareholder’s claimed injury must also be separate and distinct from any alleged injury to the company in which it holds shares. A diminution in the value of a shareholding or in distributions to shareholders, which is the result of a loss suffered by the company, is not injury which is separate and distinct from the damage suffered by the company.

Reflective Loss shall mean shareholder loss incurred in its capacity as a shareholder that is not Direct Loss.

3. For greater certainty, and for purposes of standing in ISDS,

   a. the express or implicit inclusion of shares in the definition of Investment has no effect on the requirement for Direct Loss;

   b. shareholders can own or control shares in a company, and can control a company, but as shareholders have (i) no ownership or control of company assets; and (ii) insufficient interest in company assets for standing to claim Reflective Loss;

   c. [To the extent the treaty covers indirect shareholders,] the requirement for Direct Loss applies to both direct and indirect shareholders;

   d. the requirement of Direct Loss is not satisfied by the fact that a respondent state allegedly has a treaty obligation to the covered shareholder or that the alleged obligation may have a different basis than an obligation to the company;

   e. to the extent if any that a treaty may apply to claims for loss of opportunity, once a company is constituted, the loss of an opportunity to conduct business activities carried out or expected to be carried out by the company cannot constitute Direct Loss for a covered shareholder of the company. The respective property rights of a company and a shareholder are generally defined by applicable domestic corporate law and property law.
4. Notwithstanding art. 1, when a Contracting Party directly and wholly expropriates the assets of a company, a covered shareholder who owns shares in the company has standing to claim for its Reflective Loss incurred as a result of the expropriation.

5. Notwithstanding art. 1, where there is no company remedy regime in ISDS in the applicable treaty,
   a. a covered shareholder who owns shares in a company has standing to claim for its Reflective Loss providing it demonstrates that it has sought a remedy for the company on behalf of the company in the respondent state and has been subject to a denial of justice in adjudicatory proceedings;
   b. a covered shareholder who owns or controls a company has standing to claim for its Reflective Loss providing it demonstrates that the company has sought a remedy in the respondent state to redress its injury and the company has been subject to treatment equivalent to a denial of justice in adjudicatory proceedings.

For purposes of article 5, a denial of justice in adjudicatory proceedings shall mean a denial of justice in adjudicatory proceedings under customary international law.

6. For shareholder claims under art. 4 or art. 5,
   a. [For inclusion in the provisions on consolidation]: to the extent possible, the respondent state shall have the power to consolidate claims into a single proceeding including claims under different treaties in which art. 4 or art. 5 is applicable.
   b. adjudicators shall consider interests in judicial economy;
   c. [For inclusion in the article on decisions/awards]: the award shall provide that it is made without prejudice to any right that any person may have under applicable domestic law with respect to the relief provided in the award.

7. Decisions on shareholder standing are a matter of the consent to dispute settlement of a Contracting Party and are jurisdictional in nature.

8. [For inclusion in provisions on early dismissals]: The respondent state shall have the power to obtain a decision on whether a shareholder lacks standing for some or all of its claims at an early stage of the proceedings. The respondent may also raise the scope of recoverable losses during the merits or remedies phase of a proceeding. Where the issue is raised belatedly without justification, the adjudicators may award costs [under the costs provisions].

9. [For inclusion in the article on decisions/awards]: Decisions and awards shall clearly distinguish between different corporate entities and between shareholders and companies.
4. Commentary on the first component

41. The first component can be divided into four parts. Paragraphs 1 and 2 set out the general rule: (i) a requirement that a shareholder must establish that it has suffered Direct Loss in order to have standing to claim; and (ii) a definition of Direct Loss and Reflective Loss. Paragraph 3 provides clarifications of the definition of Direct Loss. Paragraphs 4-6 set out exceptions and conditions for their application. Paragraph 6a and paragraphs 7-9 address additional elements of the rule. The commentary addresses each of these four parts in turn.

4.1. A general rule

4.1.1. A loss-based general rule

42. The loss-based rule aligns the general rule under investment treaties with approaches under domestic law and general international law. Direct Loss for a shareholder is defined as loss incurred in its capacity as a shareholder that is separate and distinct from corporate injury. Direct Loss can form the basis of a shareholder claim.

43. Reflective Loss is defined as shareholder loss incurred in its capacity as a shareholder that is not Direct Loss. Reflective Loss is not separate and distinct from corporate injury. It cannot form the basis of a shareholder claim. The distinction between direct loss and reflective loss is well established in corporate law. It is recognised to be of fundamental importance in numerous cases.

44. Reflective Loss related to company losses extends beyond the diminution of the value of shares; it extends to the loss of dividends and all other payments which the shareholder might have obtained from the company had the company not been injured. This clarification is included in the rule.

45. The terms direct loss and reflective loss are used. Reflective loss is increasingly used in international and cross-jurisdictional analysis of corporate law as well as in many domestic legal systems. It has been used in the preliminary discussions in UNCITRAL Working Group III. It was used during the extensive inter-governmental analysis of reflective loss claims in ISDS at the OECD. Some jurisdictions use different terminology to refer to shareholder losses incurred due to a company loss. In common law jurisdictions, reflective loss is sometimes referred to as “derivative” loss. Some submissions in ISDS cases use the term “indirect injury” or other phrasing.

46. The definition of Direct Loss by reference to the loss at issue and its relationship to company losses is derived from leading cases and analysis in common law and civil law jurisdictions that have set out the relationship of the shareholder loss to company loss as the critical criterion for the rule. In the recent UK Supreme Court case of *Marex*, which reaffirmed the general bar against shareholder claims for reflective loss, Lord Reed underlined that “[t]he critical point is that the shareholder has not suffered a loss which is regarded by the law as being separate and distinct from the company’s loss, and therefore has no claim to recover it.” Lord Hodge similarly emphasised that “the law’s refusal to recognise the diminution
in value of a shareholding or the reduction or loss of a distribution, which is the consequence of the company suffering loss as a result of wrongdoing against it, as being separate and distinct from the company’s loss is a principled development of company law”.  

47. In the United States, a federal appellate court has described the principle as follows:

   A stockholder of a corporation does not acquire standing to maintain an action in his own right, as a shareholder, when the alleged injury is inflicted upon the corporation and the only injury to the shareholder is the indirect harm which consists in the diminution in value of his corporate shares resulting from the impairment of corporate assets. In this situation, it has been consistently held that the primary wrong is to the corporate body and, accordingly, that the shareholder, experiencing no direct harm, possesses no primary right to sue.

In this formulation, the rule is framed in terms of the loss and the lack of standing is stated in general terms based on the relationship of the loss to company loss.

48. The Principles of Corporate Governance of the American Law Institute (ALI) recognise that although formulations of the rule can differ in some cases, all decisions are in fundamental agreement with a loss-based rule: “a wrongful act that depletes corporate assets and thereby injures shareholders only indirectly, by reason of the prior injury to the corporation, should be seen as derivative in character; conversely, a wrongful act that is separate and distinct from any corporate injury, such as one that denies or interferes with the rightful incidents of share ownership, gives rise to a direct action” (emphasis added). The US government recently described the scope of direct claims by shareholders in a large domestic law damages claim against the United States by reference to whether the harm to the shareholder is “separate from harm to the corporation”, and obtained dismissal of the shareholder claim.

54. Id. para. 108. Marex reaffirmed the case of Prudential Assurance Co Ltd v Newman Industries Ltd (No 2) [1982] Ch 204, which rejected a shareholder claim where “the deceit on the [shareholder] cause[d] the [shareholder] no loss which is separate and distinct from the loss to the company…” (emphasis added). Both cases relied on Foss v. Harbottle (1843) 2 Hare 461. See also Johnson v Gore Wood & Co., [2000] UKHL 65, [2002] 2 AC 1 at pp. 35-36 (Lord Bingham).


56. See also e.g., Gaff v. FDIC, 814 F.2d 311, 315 (6th Cir. 1987) (“Where the shareholder suffers an injury separate and distinct from that suffered by other shareholders,” or the corporation as an entity, the shareholder may maintain an individual action in his own right. … [A] diminution in the value of corporate stock resulting from some depletion of or injury to corporate assets is a direct injury only to the corporation; it is merely an indirect or incidental injury to an individual shareholder.”) (citations omitted), modified, 828 F.2d 1145 (6th Cir. 1987); Pagan v. Calderon, 448 F. 3d 16 (1st Cir. 2006) (claim against governor of Puerto Rico).

57. See Starr Int’l Co. Inc. v. United States, Principal and Response Brief for the United States, p. 30 (“A basic tenet of American corporate law is that the corporation and its shareholders are distinct entities.’ Thus, legal harms to a corporation give rise to claims belonging to the corporation itself. … [A] shareholder may under certain circumstances bring a direct claim based on harm to itself that is separate from harm to the corporation.”); Starr Int’l Co. Inc. v. United States, 856 F.3d 953 (Fed. Cir. 2017), leave to appeal (cert.) denied, (U.S. 26 Mar. 2018).
49. A loss-based rule also applies in civil law jurisdictions. In the “Dubai-Fall” case, the German Supreme Civil Court (BGH) held that shareholder recovery is limited to losses not resulting from company losses. The Court held that where a third party negligently damages a company, the shareholder cannot claim damages from the third party because this would run counter to the principle of capital maintenance (Kapitalerhaltung) and would conflict with the principle that the company’s assets are bound for the purpose of the business (Zweckwidmung des Gesellschaftsvermögens). The court gave this loss-based principle general application in barring claims for reflective loss.

50. In France, shareholders may bring claims against corporate executives or board members for “personal” losses. Such personal losses must be independent from corporate losses. Shareholder losses that are only the “corollary” of corporate losses are not personal losses.

51. The Supreme Court of Canada, in civil law cases originating from Quebec, has made clear that a shareholder must demonstrate injury independent from that suffered by the company. In Brunette, the Court held that shareholders must establish a “direct injury … distinct from that of the corporation”. The Court dismissed a shareholder claim at a preliminary stage due to the absence of an independent injury. As noted, the Court pointed out that the same rule applies in common law cases.

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58 “Dubai-Fall”, BGH 10 November 1986, WM 1987 13); see also Xiaoning Li, A comparative study of shareholder derivative claims (2007), pp. 199-200, 202 (“According to German law, only the injured [AG] company can bring an action to enforce its claims. Although the shareholders also suffer from the loss in value of shares, the loss is no more than indirect damage and the shareholders cannot bring actions directly”; same rule for GmbH type companies).


60 Art. L225-252, Code de Commerce.

61 See, e.g., Cour de cassation, chambre criminelle, Nos. 97-80664, 99-80387, 99-84855 (13 Dec. 2000) (three decisions) (rejecting shareholder claims because “la dépréciation des titres d'une société découlant des agissements délictueux de ses dirigeants constitue, non pas un dommage propre à chaque associé, mais un préjudice subi par la société elle-même”) [the loss in value of shares in a company resulting from tortious acts by its managers constitutes, not a loss belonging to each shareholder, but a loss suffered by the company itself] (author translation); Cour de cassation, chambre commerciale, No. 97-10886 (15 January 2002) ((distinguishing between a shareholder's personal injury and his/her injury caused by injury to the company ; “le préjudice invoqué par M. X, … n’étant que le corollaire de celui causé à la société, n’avait aucun caractère personnel”) [the loss claimed by Mr. X, … being only the corollary of the loss inflicted on the company, did not have any personal character] (author translation); Philippe Merle, Droit commercial : Sociétés commerciales (7th ed. 2000) § 409 (for an individual action by a shareholder, the injury must be personal, independent from the alleged injury to the company).

62 Brunette v. Legault Joly Thiffault, s.e.n.c.r.l., 2018 SCC 55, para. 31.
52. Canada has also defined direct loss in similar terms in ISDS. In *Clayton v. Canada*, Canada expressly invoked claimant failure to demonstrate the “separate and distinct” loss requirement as the basis for dismissal of a reflective loss claim:

> The [shareholder] Claimants have not met their burden under Article 1116 to demonstrate the loss or damage they incurred as investors, separate and distinct from the alleged losses of their enterprise, Bilcon of Nova Scotia. As such, their claim for compensation in their Memorial must be dismissed. 63

The case generated the most thorough publicly available submissions of government interpretations.

53. A focus on the nature of the loss focuses the inquiry on a relatively straightforward economic inquiry about the relationship of the alleged claimant loss to company loss. The determination of whether loss is Direct Loss can often be made at an early stage.

### 4.1.2. A “bright line” general rule

54. The rule sets forth a “bright line” general rule. Standing for shareholder claims for reflective loss is generally excluded as a matter of law. Adjudicators must decide if the shareholder has established Direct Loss. If not, there is no standing for the claim unless an exception applies. Adjudicators do not have discretion in applying the rule.

55. Bright line rules have benefits in terms of predictability and clarity of application; at the same time, they are less flexible than looser criteria. They can offer cost savings in adjudication and in avoiding disputes.

56. Eilis Ferran has noted the alternative possibility of resolution of the rights of multiple parties, but recognises the efficiency of a rule that applies as a matter of law:

> [I]t can be argued that, rather than classifying shareholder claims for reflective loss as being irrecoverable as a matter of law, it could be left to trial judges to evolve detailed principles for the protection of creditors and other shareholders in such cases. …. However, shareholders should not recover at the expense of creditors or other shareholders and the absolute disallowance of shareholder reflective loss claims … is an efficient way of achieving that result. 64

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63 *Clayton v. Canada*, Canada’s Counter-Memorial on Damages, para. 34 (emphasis added). See also *Alicia Grace v. United Mexican States*, Non-disputing Party Submission of the Government of Canada Pursuant to NAFTA Article 1128 (24 Aug. 2021), p. 8, footnote 25 (“A claim is direct if it concerns treatment of and loss by the shareholder that is separate and distinct from the treatment of the enterprise itself.”); *Legacy Vulcan v Mexico*, Non-Disputing Party Submission of the Government of Canada Pursuant to NAFTA Article 1128 (7 June 2021), para. 29, footnote 28 (“A claim is direct if it concerns treatment of and loss by the shareholder that is separate and distinct from the treatment of the enterprise itself. On the other hand, a claim is derivative if the shareholder was affected simply as a consequence of the treatment of the corporation. In the latter case, a shareholder does not have any independent right of action under international law with respect to reflective losses it may have suffered as a result of the treatment of the corporation.”)

64 Eilis Ferran, Litigation by Shareholders and Reflective Loss, Cambridge Law Journal, 60 [2001], pp 245-247; see also *Mid-State Fertilizer Co. v. Exchange National Bank of Chicago*, 877 F.2d 1333, 1335-36 (7th Cir. 1989) (pointing to the efficiency and fairness of company recovery); *Marex*, para. 38 (Lord Reed) (a bright line rule “has the advantage of establishing a clear principle, rather than leaving the protection of creditors and other shareholders of the company to be given by a judge in the complexities of a trial. Those complexities should not be underestimated. Even without the complications arising from the existence of concurrent claims, it would not be straightforward to
57. A bright line general rule for covered shareholder standing in ISDS may make it easier for all parties to evaluate their needs for possible coverage under contract and commercial arbitration, insurance or other forms of protection. It provides a clear basis on which to invest and contract (for covered and non-covered investors).  

58. A bright line requirement for Direct Loss may also be well-suited to a consent- or fee-based dispute settlement system. In ISDS, a beneficial owner can choose its preferred covered corporate shareholder as a claimant. Key parties including the company, major investors and others may have no access to the ISDS proceeding or be absent. They generally cannot have access as disputing parties. In *Alicia Grace v Mexico*, shareholder claimants objected to a request by alleged secured company creditors to intervene in the case and the request was denied. Basic information about the company and company creditors may generally be lacking. Consent-based tribunals have no power to obtain information from non-disputing parties.

59. In domestic law, the no reflective loss rule means that multi-stakeholder corporate disputes between all shareholders and all creditors over corporate assets principally occur in insolvency and bankruptcy contexts. Courts in such cases generally have extensive powers to gather information and determine the respective rights of multiple parties. Generally all stakeholders with claims on corporate assets can submit claims in the process. Governments that are interested in broad availability of reflective loss claims may wish to consider possible institutional reforms to ISDS to facilitate the adjudication of multi-stakeholder corporate law and finance disputes.

60. In addition, in ISDS, the tribunal fees and costs may also be being paid only by a single shareholder and the government. The company, non-claimant shareholders and company creditors may not be contributing to tribunal fees in a shareholder claim for reflective loss. The time and costs need to determine the respective rights and losses of multiple parties can be considerable even where information is fully available. A tribunal whose costs are covered by only a small fraction of the relevant parties may for example feel constrained in the time that it can devote to a full consideration of different losses. Few if any ISDS cases have engaged in extensive analysis of the distribution of reflective loss among all corporate stakeholders. A bright line general rule may be well adapted to the practical limitations on tribunals in ISDS.

establish the extent, if any, to which a fall in the value of a company’s shares was attributable to a loss that it had suffered as a consequence of the defendant’s wrongdoing. But the existence of a concurrent claim by the company would add another dimension to the difficulties.”).

65 See, e.g., *Bagdon v. Bridgestone/Firestone Inc.*, 916 F.2d 379, 384 (7th Cir. 1990) (shareholder cannot bring claim for reflective loss for itself; “Corporations are not partnerships. Whether to incorporate entails a choice of many formalities. Commercial rules should be predictable; this objective is best served by treating corporations as what they are, allowing the investors and other participants to vary the rules by contract if they think deviations are warranted.”) (emphasis in original).


67 See *Alicia Grace v. Mexico*, Procedural Order No. 4, Decision on the Ad Hoc Group of Bondholders’ Application for Leave to Intervene (24 June 2019) (denying application to intervene by bondholders who (i) claimed as secured creditors to higher priority rights to corporate assets than the claimant shareholders; and (ii) contended that any award in favour of the shareholder claimants would undermine the company’s ability to recover and thereby undermine their financial position).
4.1.3. Differences with the domestic law context

61. As set out above, the first component seeks to set out rules generally aligning ISDS with the approach under domestic law and other international law. Governments may wish to bear in mind some differences between the consideration of reflective loss claims in domestic law contexts and the ISDS context.

62. First, the claim-expanding consequences of allowing shareholder claims for reflective loss in ISDS may be broader than they would be if the law were changed to allow standing for claims for reflective loss under many domestic law systems. Investment treaties generally set forth potentially broad causes of action for unfair treatment. A contract is not required. Purely economic loss can be recovered. If those substantive provisions are interpreted to provide a basis for recovery of reflective loss, possibly contrary to government interpretations of substantive law, covered shareholders could claim for reflective loss in many cases of alleged wrongful injury to a company. In contrast, in domestic law, even if the law were changed to make reflective loss recoverable, shareholders may rarely have a cause of action against third parties that injure the company. Shareholders may need to establish that the entity injuring the company owed the shareholder a “duty of care”. There may be severe general limits on non-contractual claims for only economic loss. A commentator has noted, for example, that a change in domestic law to allow shareholder reflective loss claims would likely lead to a limited range of claims.68

63. A second difference with domestic law consideration of the issues is also significant. Domestic law cases consider whether shareholders as a class should be permitted to claim for reflective loss under the relevant circumstances. A change to domestic law to allow shareholder reflective loss claims, if accepted, would apply to all shareholders of companies under the relevant circumstances.69 In contrast, ISDS considers only whether a sub-class of shareholders can bring such claims; it is well-established that shareholders outside the sub-class cannot bring such claims. The impact in terms of differential treatment of shareholders of the same company is stronger if reflective loss claims are accepted in ISDS than it would be in the domestic law context. Concerns about equal treatment of shareholders, a significant factor in domestic decisions, are stronger in the ISDS context.70

64. A third distinction is that all constituencies will normally have access to the domestic courts for claims under domestic law. In contrast, ISDS co-exists with the domestic courts (and frequently commercial arbitration) as an additional system for certain constituencies. In some cases, companies will have the additional access to ISDS while some shareholders will not. In others, some shareholders will have the additional access to ISDS while companies will not. These aspects will be considered further in the context of work on company remedy regimes.

68 See Paul Davies, Reflecting on “Sevilleja v Marex Financial” (15 Oct. 2020) (noting that co-existing causes of action would be rare in domestic law even if shareholder reflective loss claims were allowed: referring to the “comparatively limited case where both the shareholder and company have independent causes of action against a defendant where losses overlap”), available at https://www.law.ox.ac.uk/research-subject-groups/commercial-law-centre/blog/2020/10/reflecting-sevilleja-v-marex-financial.

69 Domestic law generally excludes shareholder claims for reflective loss because, inter alia, a claimant shareholder benefits at the expense of non-claimant shareholders as well as others who rely on the company. Shareholder claims for reflective loss are rejected for all shareholders even though any shareholder could be a claimant.

70 Different rules for different groups of shareholders of the same company may create incentives for potential shareholders to reject investing in the disadvantaged class. Over time, it is possible that only unsophisticated or small shareholders may remain as domestic shareholders if other groups of shareholders have a superior status vis a vis the company, its assets and government regulation.
4.2. Clarifications

65. The model rule sets out five clarifications. The first separates the issue of coverage of shares as an investment under the treaty from the issue of reflective loss. It makes clear that the rule requires a shareholder to demonstrate Direct Loss regardless of whether shares are expressly included in a definition of investment. Some ISDS cases have relied on the inclusion of shares to find that reflective loss claims are permitted. Ascribing profound consequences in expanded shareholder rights to the mere inclusion of shares in the definition of investment may make it more difficult for governments to calibrate their commitments. The clarification ensures that governments can recognise shares as protected investments in their treaties without automatically attracting broad liability to shareholders extending far beyond normal corporate law.

66. The second clarification states that for purposes of standing in ISDS, shareholders can own or control shares in a company, and can control a company. However, as shareholders they have (i) no ownership or control of company assets; and (ii) insufficient interest in company assets for standing to claim Reflective Loss. This clarifies that general references in the definition of investment to ownership, control or interests in assets or investment do not affect the loss-based rule for shareholder standing to claim in ISDS.

67. The third clarification addresses indirect shareholders. The principal categories of direct loss to shareholders are injury to their intra-corporate rights such as the right to vote or attend meetings. Generally only direct shareholders of the company have such rights. The context of expropriation of the assets of the company is addressed in a specific exception rather than seeking to address it through the definition of Direct Loss.

68. The fourth clarification states that a shareholder right or cause of action -- or an alleged obligation or duty owed to a shareholder -- is generally not sufficient for standing in the absence of Direct Loss. The clarification reflects the general approach in domestic law. For example, in the “Dubai-Fall” case cited above, the German Supreme Civil Court found that if the shareholder’s loss was reflective, the existence of a separate legal duty to the shareholder would make no difference: the claim would be denied. In Brunette, the Supreme Court of Canada reaffirmed that shareholders must “demonstrate the existence of an independent fault and a direct injury, both of which are distinct from that suffered by the corporation”. In Basab, Inc. v. Superb Glory Holding Ltd., the Court of Final Appeal for the Hong Kong Special Administrative Region found that the focus of the rule against reflective loss must be on the type of loss claimed as opposed to the causes of action being asserted. Thus the rule applies even if the claimant can establish an independent cause of action against the wrongdoer. In Potthoff v. Morin, a US federal appellate court applied the rule barring shareholder standing to claim reflective loss to a shareholder claiming under a statutory cause of action: “when [the shareholder] incorporated [the company], he relinquished the right to seek direct legal redress under [the statute] for injuries suffered by him as [the company]’s sole shareholder and principal employee.”

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71 See “Dubai-Fall”, BGH 10 November 1986, WM 1987 13 (finding that German law would deny shareholder claim for reflective loss even though the defendant breached duties towards the shareholder).

72 Brunette v. Legault Joly Thiffault, s.e.n.c.r.l., 2018 SCC 55, para. 31 (emphasis added).


74 Potthoff v. Morin, 245 F.3d 710, 716-717 (8th Cir. 2001) (citation omitted).
corporations. The critical question is not so much with respect to the duty, but with respect to the damages recoverable consequent upon its breach".\textsuperscript{75}

69. In addition to permitting reflective loss claims based on finding that the treaty creates a separate cause of action, some ISDS tribunals have at times relied on findings that the treaty cause of action differs from the company claim in various ways. The model rule clarifies that such possible differences are irrelevant to the loss-based rule.\textsuperscript{76} The clarification excludes allowing reflective loss claims based, for example, on findings that the fundamental or essential basis of the claim is different, or that claims are juridically and analytically distinct. A cause of action may generally be necessary but is not a sufficient basis for standing under the rule.\textsuperscript{77}

70. The fifth clarification addresses the approach of the tribunal in \textit{Clayton v. Canada}.\textsuperscript{78} In \textit{Clayton}, a Canadian company (Bilcon Canada) was formed in 2002 to carry out a quarry project. The company applied for environmental approval for the quarry. The company’s application was denied. The controlling US shareholders of the company did not seek approval to carry out the project themselves. The controlling shareholders brought a claim on their own behalf under NAFTA. They complained about alleged problems in the environmental review of the company’s application. A majority of the tribunal found that the environmental review process was flawed.

71. In the damages phase, both Canada and the United States filed submissions interpreting NAFTA to exclude shareholder claims for reflective loss, noting that all three NAFTA governments are in agreement on the point. The tribunal found that shareholder reflective loss claims are in principle barred under NAFTA.

72. However, the tribunal found that an “opportunity” to obtain a satisfactory procedure was lost not by the company that sought the regulatory approval, but only by a group of companies all controlled by the claimant controlling shareholders.\textsuperscript{79} The result was that the shareholders could recover themselves essentially in the same manner as if reflective loss claims were permitted for shareholder losses arising from the wrongful denial of approval to the company’s project.\textsuperscript{80} The tribunal did not cite law or precedent


\textsuperscript{76} See, e.g., Victor Joffe et al., Minority Shareholders, (3d ed. 2009) §§ 1.151-152 ["The no reflective loss principle is not concerned with barring causes of action as such, but with barring recovery for certain types of loss. ... It is irrelevant that the duties owed by the defendant to the company and to the claimant may be different in content."] (citations omitted).

\textsuperscript{77} Some courts have distinguished cases in which a shareholder has a commercial contract with the third party that injures the company. As noted above, the model rule addresses treaty-based claims. It does not address shareholder-government contracts.

\textsuperscript{78} \textit{Clayton v. Canada}, Award on Damages (10 Jan. 2019).

\textsuperscript{79} The lost opportunity was also at times described as an opportunity to invest rather than an opportunity to obtain a satisfactory procedure. Domestic courts have rejected shareholder efforts to recharacterise their reflective loss as a “loss of opportunity”. See, e.g., \textit{Rivers v. Wachovia Corp.}, 665 F.3d 610 (4th Cir. 2011) (rejecting a shareholder effort to disguise a classic claim for a decline in the value of shares as a "lost profit opportunity" as “too clever by half”).

\textsuperscript{80} See Sylvie Tabet (General Counsel, Trade Law Bureau, Government of Canada), Shareholder Reflective Loss (undated) (power point presentation given at the Joint Webinar on Reflective Loss, slides 18-19 (stating that the \textit{Clayton} tribunal failed to apply the rule that shareholders can only bring claims for direct damages properly), available at \url{https://unctral.un.org/sites/unctral.un.org/files/media-documents/unctral/en/tabet_english.pdf}; see also Joint Webinar on Reflective Loss, available at \url{https://www.youtube.com/watch?v=EeMPWdZns3A&feature=youtu.be}.
73. The clarification addresses this possibility with a clarification for purposes of shareholder standing in ISDS. The clarification takes no position on whether claims for lost opportunities are possible under any investment treaty. If they are, it clarifies that, once a company is constituted, the loss of an opportunity to conduct business activities carried out or expected to be carried out by the company cannot constitute Direct Loss for a covered shareholder of the company for purposes of shareholder standing for claims in ISDS.

74. The clarification further provides that, for purposes of standing in ISDS, the respective property rights of a company and a shareholder are generally defined by applicable domestic corporate law and property law. Comparative corporate law scholars have identified the rules protecting corporate property from appropriation by shareholders to be fundamental rules of corporate and property law across all advanced economies examined as well as in other major jurisdictions. Respect in ISDS for corporate law and property rights under domestic law can further the goal of legal certainty and improve the prospects for investment. The inclusion of the reference to the rule applying generally provides scope for the application of additional principles if, for example, the host government profoundly modifies its applicable corporate or property law in a discriminatory manner for a particular project.

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81 See Kappes v. Guatemala, Decision on Respondent’s Preliminary Objections, (13 Mar. 2020), paras. 160-61 (noting but not deciding claims by shareholders that even if claims for reflective loss are impermissible, they could still recover under the Clayton approach to direct damages because “[l]ike the claimants in Clayton, Claimants here have lost their opportunity to develop the Tambor project, which was an opportunity of theirs rather than of [the company]”).

82 See John Armour, Henry Hansmann, Reinier Kraakman, and Mariana Pargendler, “What is Corporate Law?”, ch. 1 in John Armour et al., The Anatomy of Corporate Law (3d ed. 2017) (comparative analysis of Brazil, France, Germany, Italy, Japan, the UK, and the U.S.), pp. 5-6:

[A] firm serves, fundamentally, as the common counterparty in numerous contracts with suppliers, employees, and customers, coordinating the actions of these multiple persons through exercise of its contractual rights. The first and most important contribution of corporate law, as of other forms of organizational law, is to permit a firm to serve this coordinating role by operating as a single contracting party that is distinct from the various individuals who own or manage the firm. In so doing, it enhances the ability of these individuals to engage together in joint projects.

The core element of the firm [for this purpose] is what civil lawyers refer to as “separate patrimony.” This involves the demarcation of a pool of assets that are distinct from other assets owned, singly or jointly, by the firm’s owners (the shareholders), and of which the firm itself, acting through its designated managers, is viewed in law as being the owner. The firm’s entitlements of ownership over its designated assets include the rights to use the assets, to sell them, and — of particular importance — to make them available for attachment by its creditors. Conversely, because these assets are conceived as belonging to the firm, rather than the firm’s owners, they are unavailable for attachment by the owners’ personal creditors.” (citation omitted).

83 See, e.g., Clayton v. Canada, Canada’s Counter-Memorial on Damages (9 July 2017) para. 26 (“Awarding damages to shareholders for losses incurred by enterprises undermines one of the most fundamental rules of corporate law in all three NAFTA Parties. Allowing shareholders to recover reflective losses under Article 1116 will weaken the corporation’s separate legal personality, create unpredictability for investors, creditors, banks, and others who participate in the foreign direct investment market, create unfair conditions of competition among these different sorts of investors, and hence, inevitably decrease the opportunities for investment in the NAFTA Parties.”)
4.3. Exceptions

4.3.1. Expropriation

75. A government may directly expropriate a company by acquiring its shares from the shareholders. Such action can cause Direct Loss to shareholders who lose their shares.

76. A government may also directly expropriate a company by appropriating essentially all of a company’s assets. The company can suffer Direct Loss: it no longer owns the assets that the government has appropriated. It normally has a claim for expropriation of its assets if compensation is insufficient. Shareholders also suffer loss. However, it arises from the company loss of its assets. The shareholder loss is not separate and distinct from the company loss. It does not constitute Direct Loss under the general model rule.84

77. Article 4(a) establishes the expropriation of the company’s assets as an exception to the requirement for Direct Loss for shareholder standing. Covered shareholders exceptionally have standing to claim for their Reflective Loss.

78. This exception may give rise to possible multiple claims for the same injury. The company may claim. Different groups of covered shareholders may claim. However, the direct expropriation of assets is relatively rare. Moreover, where essentially all of the company’s assets are transferred to the government, the company may have difficulty bringing a claim or may face obstacles in the domestic courts or in arbitration. Consideration of possible approaches to company remedy regimes is relevant to approaches to expropriation.

4.3.2. Denial of justice in adjudicatory proceedings in the host state

79. Paragraph 5 sets out two exceptions. They apply where there is no applicable company remedy regime in ISDS. The general primacy of the company in recovering for company injury is recognised.

80. Both exceptions apply only when there has been a denial of justice in adjudicatory proceedings in the host state. The first situation addresses situations where the domestic courts fail entirely to uphold their role with regard to corporate governance. The rule follows domestic law in generally recognising that, unless company management is tainted by a conflict of interest, it is for company management, not individual shareholders, to decide on how to deal with the claim for its injury.

81. However, in some cases, the corporate governance machinery in the company can break down. For example, the board of directors may improperly fail to cause the company to bring a claim against a third party that has injured the company because members of the board have a conflict of interest vis-à-vis the third party. The failure to bring a company claim injures the company directly. A shareholder does not suffer direct loss from the company failure to claim. However, in such situations, a shareholder can seek to act on behalf of the company under domestic law providing for shareholder derivative actions in the domestic courts.

82. The exception generally leaves the decision in this area to the domestic courts. Many legal systems place significant legal and practical barriers on derivative actions for various reasons. Derivative actions interfere with the normal governance of the company by its board or by a majority of shareholders, and

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84 Government expropriation of all the assets of the company may be considered as direct loss for shareholders under customary international law. However, as noted the model rule does not seek to reflect customary international law concepts and no view is expressed in that regard. Rather than seek to adjust the basic loss-based rule to include expropriation of company assets as direct shareholder loss, the model rule addresses expropriation of company assets as an exception to the loss-based rule. This permits a straightforward general rule.
raise other concerns. They can impose reputational and other costs on the company. Limits on the rights of minority shareholders and rejections of derivative actions are thus not unusual. The operation of these rules is part of the general environment for investment and varies between jurisdictions including between advanced economies. However, if the shareholder demonstrates that it has suffered from a denial of justice in adjudicatory proceedings in connection with a claim of this type, the exception permits a claim for Reflective Loss in ISDS.

83. This exception would be available to covered shareholders including minority shareholders. A 20% minority shareholder confronted with collusion between the majority domestic shareholder and government, to the detriment of the company, would have potential access to ISDS for its reflective loss. It would need to seek to enforce the company’s interests in the domestic courts. If the shareholder suffers from a denial of justice in adjudicatory proceedings in this context, it would have standing for a claim.

84. The rule defines a denial of justice in adjudicatory proceedings by reference to customary international law. The requirement of a denial of justice in adjudicatory proceedings limits the scope for ISDS tribunal evaluation of the quality of company recourse in the domestic courts. This may be desirable for several reasons. First, as consent-based tribunals with limited jurisdiction, ISDS tribunals may not well situate to evaluate the company’s perspective. The shareholder may provide or have limited information about the company. The company, its board of directors, its creditors and its shareholders generally are not before the tribunal.

85. Second, the claimant shareholder’s interest in claiming reflective loss may be a part cause of company inaction. Rules that allow shareholders to claim for themselves based on alleged impediments to company recovery can exacerbate the risk of company passivity, to the detriment of other investors. In contrast, where access to reflective loss is not available, shareholder interests are aligned with company interests and there may be more interest in company recovery. Third, ISDS tribunals compete in policy terms with the domestic courts as dispute settlement options for governments; this may affect ISDS tribunals’ perceptions of the quality of recourse for claimants in domestic courts as compared to ISDS.

86. The domestic courts are thus subject to a limited degree of review of their role in upholding their national standards of corporate governance. Together with the growing competition for investment, this can provide incentives to strengthen corporate governance regimes.

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An example of recent state practice setting out government views about the contours of denial of justice in adjudicatory proceedings is set out in Lion Mexico Consolidated L.P v. Mexico, Submission of the United States of America (21 June, 2019), paras. 6-9, 11-14:

A denial of justice may occur in instances such as when the final act of a State’s judiciary constitutes a ‘notoriously unjust’ or ‘egregious’ administration of justice ‘which offends a sense of judicial propriety.’ More specifically, a denial of justice exists where there is, for example, an ‘obstruction of access to courts,’ ‘failure to provide those guarantees which are generally considered indispensable to the proper administration of justice, or a manifestly unjust judgment.’ Instances of denial of justice also have included corruption in judicial proceedings, discrimination or ill-will against aliens, and executive or legislative interference with the freedom of impartiality of the judicial process. At the same time, erroneous domestic court decisions, or misapplications or misinterpretation of domestic law, do not in themselves constitute a denial of justice under customary international law. … [T]he actions of domestic courts are accorded a greater presumption of regularity under international law than are legislative or administrative acts… It is well-established that the international responsibility of States may not be invoked with respect to non-final judicial acts, unless recourse to further domestic remedies is obviously futile or manifestly ineffective. (citations omitted).

Mexico’s interpretation of the denial of justice standard in its submissions is only indirectly available as summarised in the award (which also provides the tribunal’s interpretation). See Lion Mexico Consolidated L.P v. Mexico, Award (20 Sept. 2021).
87. The second exception in paragraph 5 sets out a narrow ground for shareholder claims for reflective loss due to the status of the company. Where the company brings the claim in the domestic courts but is subject to treatment akin to a denial of justice in adjudicatory proceedings, covered shareholders are exceptionally permitted to claim for their reflective losses.

88. The exception in art. 5(b) applies to companies owned or controlled by a foreign covered shareholder. The requirement of ownership and control is similar to requirements in typical company remedy regimes. Issues and potential provisions relating to the standard and proof necessary for a shareholder to establish that it has control or ownership are postponed until they are considered in that context.

89. The requirement that the company seeks to bring the claim for itself is in line with the general view that recourse for the benefit of the company rather than for the benefit only of some individual shareholders is the normal solution to company injury. Company injury is best resolved by possible company remedies that give relief to all shareholders and creditors of the company. However, where company recourse is subject to treatment akin to a denial of justice in adjudicatory proceedings in the domestic courts and there is no company remedy regime in the applicable treaty, a shareholder claim for reflective loss is exceptionally available. The standard is one “equivalent to” denial of justice in adjudicatory proceedings because that law is not directly applicable to treatment of a domestic company by its “own” government.

90. As noted, the rule provides that the art. 5 exceptions allowing claims for reflective loss are only available where the treaty does not have a company remedy regime. The requirement is the absence of a company remedy regime. Where there is such a regime, no claim for reflective loss is permitted even if the company remedy regime is not applicable.

91. Along with all of the proposed rule, but in particular here, it may be helpful to consider the proposed framework in conjunction with a possible company remedy regime and its design. The NAFTA governments, for example, have included company remedy regimes in most if not all of their treaties since 1994. They have not recognised the existence of any exception allowing for shareholder claims for reflective loss. Neither exception set out in art. 5 has been recognised. In the circumstances in art. 5(a), a shareholder has no claim for reflective loss under the existing general government interpretations. In the circumstances in art. 5(b), the controlling shareholder is given access to a claim for a company remedy in ISDS. However, it has no claim for its own reflective loss for itself, contrary to the rule in art. 5(b).

92. Similarly, in Marex, the UK Supreme Court overruled previous cases that had introduced exceptions allowing shareholder claims for reflective loss where the company is legally or factually unable to bring the claim. It found that a possible derivative claim on behalf of the company is preferable to allowing recovery only by a claimant shareholder for itself. A company remedy regime may similarly be preferable to allowing shareholder claims for reflective loss in ISDS in the circumstances covered by the two exceptions in article 5.

4.4. Other elements of the first component

93. The rule addresses several other issues. In some cases, it refers to the inclusion of rules on shareholders claims that could be integrated in rules governing certain procedural issues more generally. The rules could also be included in the shareholder claims provisions.

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86 This text refers to the general positions taken by the governments to date in public submissions. Government recognition of exceptions in future cases is possible.
4.4.1. Consolidation and judicial economy

94. The exceptions in the rule allowing for certain shareholder claims for Reflective Loss can give rise to multiple claims. The rule provides that for such claims, the respondent state has the power to consolidate claims into a single proceeding including for claims under different treaties/cases in which art. 4 or 5 is applicable. Consolidation would be possible for cases/treaties in which the model rule applies. Disputing parties would accept the rules under which governments have agreed to resolve disputes, including the consolidation rules. The mechanism for such consolidation can addressed as part of general discussions over consolidation.

95. As noted, the treaty shopping power generated by the availability of reflective loss claims can allow beneficial owners to attribute claims to shareholders that are covered under unreformed treaties. The treaty shopping power generated by ability to attribute reflective loss claims is a general issue for the effectiveness of reforms that may be unattractive to beneficial owners and claimants. \(^87\) It can be considered further in discussions both over reflective loss and other reforms.

4.4.2. Nature of shareholder standing as a jurisdictional issue

96. The model rule addresses reflective loss from the perspective of standing. It states that shareholder standing is a jurisdictional issue in ISDS. It is described as a matter of the consent to arbitrate of a Contracting Party. An explicit resolution of the nature of the issue avoids lengthy litigation over whether the issue is jurisdictional.

97. Characterisation of the issue as one of jurisdiction has several consequences. Jurisdictional issues are subject to review even under narrow regimes for review. This provides governments, claimants and a reviewing body with the opportunity to evaluate the decision of the first instance tribunal on the issue. This may be valuable where rules modify existing approaches or may significantly affect the scope of jurisdiction.

98. The characterisation of the issue can be further considered in the context of discussions about the scope for review under an appeal system. The rule provides that the issue of recoverable loss can also be raised and decided at the merits or remedies stage of the case. In some cases, it may emerge or become clear during the course of the proceedings as more facts become known.

4.4.3. Availability of early resolution

99. The rule refers to inclusion of a government power to obtain a ruling on a shareholder claim for reflective loss at a preliminary stage. The rule could be included in general provisions on preliminary objections. The nature of a shareholder’s loss can often be resolved in decisions early in a case.

100. Many of the leading cases in the field have terminated reflective loss claims at a preliminary stage. Many cases can be entirely resolved. Where both direct loss and reflective loss are at issue, cost savings can be achieved by narrowing the issues.

101. Arbitral hesitation or refusal to identify or to dismiss reflective loss claims at an early stage means that they remain in the case. In addition to potentially creating confusion in the case at hand, it can encourage further submissions of concurrent individual and derivative claims for the same injury in additional cases.

4.4.4. Instruction to distinguish clearly between corporations and their shareholders

102. The rule includes an instruction to adjudicators to distinguish clearly between corporations and their shareholders. Some cases refer interchangeably to shareholders and corporation. Shareholders and corporations are sometimes grouped together into a single defined definition. The respective rights and actions of each become blurred. A corporation and its shareholders normally do not own the same assets. They rarely have all the same creditors. The distinction between the legal personality, rights and obligations of each is a core component of corporate law and finance. In the administrative law context, a company request for a regulatory approval is generally not the same as a request by shareholders.

103. Shareholders and their beneficial owners can have an interest in confusion in this area which can benefit them at the expense of creditors. Beneficial owner and claimant counsel in ISDS may have an interest in encouraging these tendencies. Shareholder liability for corporate debts has not been at issue in ISDS so confusion between companies and shareholders, and their respective assets, generally provides only benefits to claimant shareholders.

104. The confusion has also characterised cases under treaties that provide for company recovery regimes. In Feldman, this type of confusion affected the award, which had to be corrected to provide for payment to the company rather than a shareholder. See Feldman v Mexico, Correction and Interpretation of the Award (13 June 2003).
5. Additional issues for consideration

105. There are a range of additional issues that may merit consideration by governments and others in the context of evaluating options to address shareholder claims for reflective loss and related issues. This section highlights some additional issues of note.

5.1. Public law type violations and remedies for companies and shareholders

106. Investment treaties are often recognised as bearing similarities to a public law system. Government administrative action and its legality are often core issues. Issues akin to domestic public law frequently raised in current ISDS proceedings include disputes over permits and licenses, disputes over the interpretation of domestic law including the legality of investment, and claims of procedural failings relating to due process.

107. However, the two regimes today apply different remedies. Remedies in domestic law for violations of public law are generally non-pecuniary. Claimants may obtain an injunction or annulment of illegal government action, but not damages. A range of policy reasons generally limit public law remedies to non-pecuniary remedies.

108. The availability of shareholder claims for reflective loss, the use of damages as the normal remedy in ISDS and the interpretation given to certain investment treaty provisions has made damages available in many public law-type contexts to covered shareholders in ISDS but not to a domestic company. This can transform the nature of domestic public law and may affect the incentives of governments and of those injured by governments. Limitations on shareholder claims for reflective loss would reduce the effective transformation of public law injuries to companies into damages claims by shareholders in ISDS.

109. In the context of company remedy regimes, damages for the full scope of company losses can increase government exposure to damages claims in comparison to amounts claimed by individual covered shareholders. Under current approaches to applying damages as a general remedy and to evaluating them,


90 See Clayton v. Canada, Dissenting opinion of Professor Donald McRae (dissenting on Award on jurisdiction and liability) (10 Mar. 2015), para. 48 (expressing concern about the transformation of public law cases into damages claims: “Failure to comply with Canadian law by [an environmental] review panel now becomes the basis for a NAFTA claim allowing a claimant to bypass the domestic remedy provided for such a departure from Canadian law. This is a significant intrusion into domestic jurisdiction and will create a chill on the operation of environmental review panels. In the past, if they made an error – exceeded their jurisdiction or failed to comply with the law – they would have had their recommendations ignored by the governments to which they were made or overturned on review by a federal court. If the majority view in this case is to be accepted, then the proper application of Canadian law by an environmental review panel will be in the hands of a NAFTA Chapter 11 tribunal, importing a damages remedy that is not available under Canadian law.”)
the amounts at issue could be very substantial. Consideration of applicable remedies can also be considered in the context of company remedy regimes. Most investment treaties address remedies only for expropriation. The term company remedy regime is used herein to allow for consideration the possible application of remedies other than damages for companies, in particular in the context of scenarios akin to narrow public law determinations with regard to particular companies.

110. These aspects may raise further issues for consideration by the Working Group with regard to shareholder and company claims and remedies.

5.2. Waivers of other claims

111. A number of recent treaties include waiver provisions to limit concurrent claims as a general matter. A claimant must file a written waiver of any right to initiate or continue, before any court or administrative tribunal under the law of a Contracting Party, or any other dispute settlement procedures, any proceeding with respect to any measure alleged to constitute a breach. Such provisions are applicable to all claims.

112. Where a company remedy regime is included, and in particular where a derivative type action is included, the waiver requirement applies to the company. For example, in the CPTPP, the controlling shareholder is required to obtain and provide a written waiver from the company of any right to initiate or continue, before any court or administrative tribunal under the law of a Contracting Party, or any other dispute settlement procedures, any proceeding with respect to any measure alleged to constitute a breach.

5.3. Application to claimants other than shareholders

113. It will be important also to consider the possible application of a general no reflective loss principle to claims for reflective loss by creditors and other non-shareholder investors. While domestic law is uniform in generally barring shareholder claims for reflective loss, it varies with regard to claims by creditors.

114. In the United States, for example, the bar on claims for reflective (derivative loss) has been applied to all investors in companies. In Mid-State Fertilizer Co. v. Exchange National Bank of Chicago, a US federal appellate court recognised that many parties invest in a company: shareholders, lenders, suppliers, employees who invest human capital, and others. For all of these investors in the company, claims for reflective loss are barred because the company is the proper and efficient claimant:

Good reasons account for the enduring distinction between direct and derivative injury. When the injury is derivative, recovery by the indirectly-injured person is a form of double counting. "Corporation" is but a collective noun for real people -- investors, employees, suppliers with contract rights, and others. A blow that costs "the firm" $ 100 injures one or more of those persons. If, however, we allow the corporation to litigate in its own name and collect the whole sum (as we do), we must exclude attempts by the participants in the venture to recover for their individual injuries. A fire that causes $ 100 worth of damage to "the corporation", and therefore reduces the value of investors' stock by $ 100, does not cause a total injury of $ 200 -- the net loss is $ 100, and everyone is made whole by an award of that sum to the firm. To avoid double counting courts must either restrict recoveries to the directly-injured party or attempt to apportion the recovery according to who bears the effects: say, $ 60 to equity investors, $ 20 to debt investors, $ 10 to employees with specialized skills, $ 10 to persons who leased property to the firm.
Divvying up the recovery would be a nightmare, making the task of awarding damages to "indirect purchasers" in antitrust law easy by comparison. Why undertake such a heroic task when recovery by the firm handles everything automatically? -- for investors, workers, lessors, and others share any recovery according to the same rules that govern all receipts. Recovery by the firm, followed by division according to entitlements, is especially important when the firm has landed in bankruptcy. Suits by shareholders, guarantors, and the like may well be efforts to divert the debtor's assets -- to pay off one set of creditors … while keeping the proceeds out of the hands of the firm's other creditors….

Guarantors must be treated as creditors. When they suffer direct injury -- injury independent of the firm's fate -- they may pursue their own remedies. Those whose injury is derivative must take their place in line as creditors in the bankruptcy action (or outside of it), dependent now as before on the success of the firm in which they invested.91

115. In contrast, in *Marex*, the UK Supreme Court recently limited the no reflective loss principle to shareholders, finding it inapplicable to creditors. The Court grounded an absolute bar against such claims by shareholders on the particular relationship of shareholders to the company under corporate law. As noted, it overruled exceptions, finding that shareholders that incur reflective loss have no recoverable loss as a matter of law. However, it found that creditors have a different relationship to the company. It overruled a number of prior cases applying the no reflective loss principle to creditors. Like shareholders, as noted above, creditors may often face difficulties in domestic law in stating a cause of action against third parties that injure the company and cause only financial loss to the creditor.

5.4. Application to enterprises with juridical personality other than companies

116. As noted above, the draft rule refers to shareholders and companies to address the core context in the first instance. Other forms of business organisations may give rise to analogous issues.

117. Recent treaties often use a broadly defined notion of enterprise and a sub-category of enterprises that have juridical personality. The notion of juridical personality generally means that an entity has its own assets and liabilities, separate from those of its owners. A similar approach could be adopted in model rules to provide for rules extending beyond companies to cover other entities with legal personality.

91 *Mid-State Fertilizer Co. v. Exchange National Bank of Chicago*, 877 F.2d 1333, 1335-37 (7th Cir. 1989); see also *Pagan v. Calderon*, 448 F.3d 16, 29 (1st. Cir. 2006) ("As is the case with shareholders, creditors do not have standing to sue in their personal capacities unless the alleged misconduct causes harm to them separate and distinct from the injury inflicted upon the debtor corporation."); *Landune International Ltd v Cheung Chung Leung [2006] 1 HKLRD 39* (Court of Appeal of Hong Kong SAR).