

In this Part, I will introduce *i. subject matter of the research* – “shareholder claims for reflective loss (SRL)” – which elaborates research objectives and questions; *ii. methodology* – various legal methods – which helps conduct profound research on the subject matter of the research in company law and international investment law; and *iii. structure of the research*, which provides information about the structure of the book.

## I. SUBJECT MATTER OF THE RESEARCH<sup>1</sup>

This book will analyse different treatments and/or approaches to SRL in company law and international investment law. Shareholders can suffer a reflective loss *incurred through a direct loss to the company which results in a decrease in the value of their shares*.<sup>2</sup> Examples of such reflective losses can be damage to the property (assets) of the company by wrongful conduct of the directors of the company or a breach of the contractual or any other legal obligations by a third party, which results in a decrease in the value of the assets of the company and, correspondingly, the value of the shareholders’ shares.<sup>3</sup> Consequently, shareholders suffer financial (economic) losses, which influence the value of the shares negatively, resulting in fewer dividends or profits for shareholders.<sup>4</sup>

SRL is treated in a distinct manner under company law and international investment law. Company law generally prohibits shareholders from bringing direct claims for the recovery of reflective loss, which is also known as the *no reflective loss rule*.<sup>5</sup> Even though shareholders can claim direct loss of their rights as shareholders<sup>6</sup> under company law, they are not permitted to do so for reflective losses suffered due to the direct loss caused to the company. Therefore, based on the *no reflective loss rule*, only the company can claim compensation for such a loss.<sup>7</sup> In other words, when a company suffers a direct

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1 Hereinafter, “research” may be referred to as “dissertation”, “research project” or “book”.

2 See de Jong, B. J. (2013) Shareholders’ Claims for Reflective Loss: A Comparative Legal Analysis. *European Business Organization Law Review*, 14 (1), pp. 97-118, p. 99.

3 The correlation between the assets of the company and the value of shares has been subject to debate in the ISDS case law. See Part III of this book. Gaukrodger, D. (2013) *Investment Treaties as Corporate Law: Shareholder Claims and Issues of Consistency*. OECD, Working Paper No. 2013/3, OECD Publishing, Paris, France.

4 See Lee Suet Lin, J. (2007) Barring Recovery for Diminution in Value of Shares on the Reflective Loss Principle. *Cambridge Law Journal*, 66 (3), pp. 537-558; See Chaisse, J., & Li, L. Z. (2016). Shareholder Protection Reloaded Redesigning the Matrix of Shareholder Claims for Reflective Loss. *Stanford Journal of International Law*, 52 (1), pp. 51-94, p. 53.

5 See OECD, FOI Roundtable 18, Summary of discussion, p. 5 (March 2013). Gaukrodger (2013) *supra* note 3, pp. 7-8.

6 *Ibid.*

7 For analysis of national company law and general international law relevant to shareholder claims, Gaukrodger (2013) *supra* note 3, pp. 15-24.

loss due to a wrongdoer's wrongful actions, only the company is entitled to bring a claim against the wrongdoer for such a loss.<sup>8</sup>

In contrast, international investment law generally allows shareholders to bring direct claims for the recovery of reflective loss. Investment arbitral tribunals in investor-State dispute settlement (ISDS)<sup>9</sup> have constantly held that shareholders can bring direct claims for the recovery of reflective losses based on the protection of foreign investment<sup>10</sup> provided by investment treaties.<sup>11</sup> However, this permissive approach to the issue of SRL in international investment law also causes concerns by the governments.<sup>12</sup> This means that long-standing positions forming a *locus communis* (*commonplace*) of ISDS for the availability of SRL are not always relevant<sup>13</sup> or supported by the governments in

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8 The same wrongdoer may breach a duty to a shareholder, which is beyond the subject matter of the research. The shareholder's personal duties are a different and complex subject that will not be explored in this book. Since the reflective loss rule does not distinguish between shareholder's personal duties' nature and source, only the reflective loss rule is dealt with in this book. However, shareholders' direct claims are occasionally examined under company laws in this book, since the national courts sometimes address them in the analysis of the reflective loss rule.

9 See, generally, United Nations Conference on Trade and Development (UNCTAD) (2013), *Recent Developments in Investor-State Dispute Settlement (ISDS) No.1*. Investor-State dispute settlement (ISDS) is a system that allows foreign investors to sue countries for specific State actions that influence foreign direct investment (FDI). This system is most commonly implemented through international arbitration between a foreign investor and the State receiving FDI. Therefore, as the focus of the book is on "Investor-State Arbitration", the terms used such as "Investor-State Dispute Settlement" ("ISDS") or "ISDS tribunals" or "Investment Tribunals", "Investment Arbitral Tribunals" or "Investor-State Arbitration" ("ISA") or "Arbitral Tribunals" mean international arbitration between a foreign investor and the host State.

10 See FOI Roundtable 18, Summary of discussion, p. 8. The Roundtable also expressed interest in additional policy analysis of SRL from a corporate law perspective, including their impact on investment, creditors, and non-claiming shareholders. See Eilís Ferran, *Reflective Loss* (presentation to FOI Roundtable, 16 October 2013); See also Gaukrodger, D. (2014) *Investment Treaties and Shareholder Claims for Reflective Loss: Insights from Advanced Systems of Corporate Law*, OECD Publishing, Paris, France p. 9.

11 States have entered an impressive number of investment treaties that constitute international investment law. These investment treaties form a complex web of international investment agreements (IIAs) commonly recognized as international investment law, whether Bilateral Investment Treaties (BITs), Multilateral Investment Treaties (MITs, which can be abbreviated or called differently depending on the name of the treaty), or specific investment chapters (provisions) about the protection of foreign investment in Free Trade Agreements (FTAs) – that provide a framework for foreign direct investments (FDI), which are the business transactions involving the transfer of tangible and intangible assets, including capitals and services into another country with the aim of generating wealth. "IIAs" and "Investment treaties" are used as interchangeable terms in this book. I will refer to the IIAs in footnotes using its full or abbreviated name in the following format: "year, states and type of investment treaty – BIT, FTA or MIT etc."

12 See United Nations Commission on International Trade Law Working Group III (Investor-State Dispute Settlement Reform) 38th session Vienna, 14-18 October 2019 "Possible reform of investor-State dispute settlement (ISDS) Shareholder claims and reflective loss", Note by the UNCITRAL Secretariat on shareholder claims and reflective loss, A/CN.9/WG.III/WP.170, 9 August 2019; See also, Douglas, Z. (2009) *The International Law of Investment Claims / Zachary Douglas*. Cambridge, UK: Cambridge University Press, p. 455, at para. 854.

13 See Gazzini, T. (2009) General Principles of Law in the Field of Foreign Investment. *The Journal of World Investment & Trade*, [Online] 10 (1), pp. 103-119.

ISDS. This general position taken by ISDS for the availability of SRL in international investment law contrasts with the position of national courts in company law.<sup>14</sup>

Therefore, the objective of this book is, first, to analyse the different treatments and/or approaches to SRL as well as reasons for such different treatments in company law and international investment law. Second, I will also reveal the possible exceptions and/or alternative legal avenues for recourse to seeking compensation for reflective losses by shareholders. Third, I will further explore the concerns arising from the interaction of these distinct legal areas on the question of SRL, if there are any. Finally, I will analyse all feasible options to mitigate (or avoid) concerns arising from such an interaction while aligning with the principles (policies) of company law and international investment law and make suggestions for addressing a compromise on the question of SRL, if necessary.

To achieve this objective, I will answer the following main research question: *What are the reasons for the different treatment of SRL under company law and international investment law, and does this different treatment on SRL cause concerns arising from the interaction of these two distinct areas of law and – if any – what might be suggested to mitigate (or avoid) concerns and address a compromise on the question of SRL?*

For this purpose, the main research question also includes the following sub-questions that provide a comprehensive analysis of the components of the main research question:

- 1) *What are the reasons (concerns) against SRL under company law, and how are these reasons (concerns) justified from legal and economic perspectives?* The answer to this sub-question will allow us to understand why and how company law generally prohibits SRL.
- 2) *What are the reasons (rationales) for the allowance of SRL by ISDS in international investment law, and how is this regulated?* The answer to this sub-question will allow us to understand why and how SRL is allowed under international investment law.
- 3) *Do the different treatments of or approaches to SRL cause concerns in the interaction of company law and international investment law, and, if so, how can such concerns be mitigated (or avoided (solved))?* The answer to this question will allow us to find out possible concerns in the interaction of two distinct areas of law and understand what might be suggested to mitigate (or avoid) concerns and address a compromise on the question of SRL.

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14 As the terminology varies in the literature, “national law” and “domestic law” are used interchangeably.

## II. METHODOLOGY

To answer the aforementioned research questions, I will use a variety of legal methods, mainly doctrinal methods of legal research, comparative methods of legal research, and economic analysis of law.

First, the doctrinal method of legal research is described

“as a ‘synthesis of rules, principles, norms, interpretive guidelines, and values’ which explains, makes coherent, or justifies a segment of the law as a part of the larger system of law”.<sup>15</sup>

This method of law will generally help me to analyse the rules, norms, and principles developed by legislators, investment treaty drafters, the national case law, and the ISDS case law which arrange, order, and systematize legal propositions<sup>16</sup> or approaches to the question of SRL. It will also allow me to employ the inductive method of reasoning, which builds a theory on facts and law resulting in the accommodation of different opinions, viewpoints, and priorities<sup>17</sup> in the assessment of SRL in two distinct areas of law.

Second, the comparative method of legal research is a

“systematic exposition to rules, procedures as well as institutions and their application prevalent in one or more legal systems or subsystems with a comparative evaluation after estimation of their similarities and differences as well as implications”.<sup>18</sup>

This method of law may apply to “*doctrinal or non-doctrinal, theoretical, or fundamental, historical, or contemporary, qualitative, or quantitative analysis*”.<sup>19</sup> I will mainly use doctrinal qualitative analysis,<sup>20</sup> which will specifically allow me to explain the aims and objectives of different treatments or approaches to SRL in company law and international investment law. In this regard, the identification of relevant legislation,

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15 See Bhat, P. I. (2020) *Idea and Methods of Legal Research*. 1st ed. New Delhi: Oxford University Press; See also, Mann, T. (2010) *Australian Law Dictionary*. Oxford University Press, South Melbourne, Victoria, Australia, p. 197, cited in: Watkins, D., & Burton, M. (eds.) (2013) *Research Methods in Law*. Routledge, p. 9.

16 Ibid., p. 145; See also, Jain, S. N. (2010) Doctrinal and Non-doctrinal Legal Research. In S. K. Verma & A. Wani (eds.), *Legal Research and Methodology*. 2nd ed. Indian Law Institute, New Delhi, India, p. 68.

17 See Bhat (2020) *supra* note 15, p. 149.

18 Ibid., p. 269.

19 Ibid.

20 See McConville, M., & Chui, W. H. (eds.) (2017) *Research Methods for Law*. 2nd ed. [Online]. Edinburgh: Edinburgh University, p. 24.

case law, and secondary materials in law will help reveal differences in the treatment of SRL and reasons for such different treatments under company law and international investment law as well as concerns arising from the interaction of these two distinct areas of law on the question of SRL.

Comparative methods of legal research can also be horizontal and vertical.<sup>21</sup> Based on the horizontal comparative method of legal research, I will compare different company law systems on the question of SRL, assessing the relevant merit and development of the approach to SRL in relation to one another. Stemming from the distinct principles, approaches, and institutions, legal systems can be grouped into five main legal systems in the world: common law, civil law, socialist law, religion-based law, and mixed legal systems.<sup>22</sup> However, considering the common and civil law legal systems to be the most influential and principal legal systems in the world,<sup>23</sup> I will focus on the analysis of company laws based on the jurisdictions stemming from the common and civil law systems. Given the fact that the company law rules of the United Kingdom and the United States, for the common law system, and the company law rules of Germany and France, for the civil law system, are considered advanced or doctrinally well developed,<sup>24</sup> I will thus mainly analyse company laws with respect to the treatment of SRL based on these four jurisdictions (United Kingdom, United States, Germany, and France).

Moreover, I will be able to compare the typical provisions of investment treaties and the ISDS case law for the treatment of SRL in international investment law. I will use the most relevant investment treaties and the ISDS case law to achieve the objective of my research in international investment law. The relevant investment treaties and ISDS case law will include relation to the jurisdictions of company law systems to be researched in this book but will not be limited to them.

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21 See Bhat (2020) *supra* note 15, p. 272.

22 *Ibid.*, p. 270.

23 “A legal system or legal tradition is a set of deeply rooted historically developed legal norms, principles, institutions and processes being applied in a specific jurisdiction or community”: See Burazin, L. et al. (2022) Legal Systems as Abstract Artifacts. In *The Artifactual Nature of Law*. [Online]. Cheltenham, UK: Edward Elgar Publishing, p. 2; See also, Embley, J., Goodchild, P., & Shephard, C. (2020) *Legal Systems and Skills: Learn, Develop, Apply*. 4th ed. Oxford University Press, Oxford, United Kingdom, p. 36.

24 This book will primarily examine the national company laws of the United States, United Kingdom, Germany, and France, as they include the most advanced and better developed rules in this area of law. These company law systems have extensively developed doctrines that contain a framework, set of rules, theories, or principles or procedural mechanisms, often established through precedent or jurisprudence that are widely followed in a field of company law. Consequently, it provides a broader framework for legal analysis and interpretation in the SRL. Therefore, I will examine the company law rules in the examples of these countries (jurisdictions), which will be referred to as “company law (s)” or “company law system (s)” depending on the meaning of the sentence. The national company law rules of New Zealand, Hong Kong, Singapore, Brazil, Japan, and the Czech Republic will mainly be addressed in the footnotes of this book if I find them relevant and necessary to mention, as such jurisdictions may have had an impact on this issue. I have not analysed other company law systems, including Dutch law, either because those systems have not analysed this issue in depth or because the analysis of this issue contains similar conclusions to those reached in the company systems analysed in this book.