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THE FOREIGN SOVEREIGN IMMUNITIES ACT:
A CONSIDERATION OF THE THIRD CLAUSE OF 1605(a)(2)

The concept of sovereign immunity is based on the idea of protecting the dignity of sovereign entities, a principle worthy of continuation. However, when it is applied unfettered, it has the possibility of obstructing justice. Until 1952 the United States courts, under State Department consent, applied immunity to all sovereigns that were brought before them. In 1952, the State Department issued a letter drafted by Jack B. Tate which introduced the theory of restrictive sovereign immunity to U.S. courts. The Tate letter held that governments brought before U.S. courts must still be considered immune from jurisdiction for their public acts (jure imperii), but must be held accountable for their private acts (jure gestionis).¹

The Tate letter was an attempt to allow governments to go about their administrative responsibilities unhindered, but allow private parties to have recourse for wrongs committed by a government outside those administrative responsibilities. Although it was a step in the right direction, it was not all that was needed. The area encompassing public and private acts was left extremely vague and open.

Congress, recognizing that further codification was necessary, passed the Foreign Sovereign Immunities Act (FSIA) in 1976. The purpose of the act is to lay down a standard that can be uniformly applied to cases involving a foreign government which claims to

be immune from jurisdiction. Obviously the FSIA cannot give extraterritorial jurisdiction, but it does provide the exceptions of immunity applicable in U.S. courts. Although the purpose of the act is on target, the FSIA is criticized for allowing ambiguity to run rampant within the act itself. To understand the problems arising from the application of the FSIA to commercial actions brought to court, the purpose of the act needs to be examined more closely. Two points within the third clause of subsection 1605(a)(2) in particular need to be analyzed: what constitutes 1) a commercial activity, and 2) a direct effect in the United States.

Introduction to the FSIA

As stated earlier, one of the purposes of the restrictive theory of immunity is to bring governments to a position of equality in the marketplace. One of the purposes of the FSIA is to codify the application of that principle. Within subsection 1605(a)(2) the conditions that are necessary for a sovereign to lose its immunity through a commercial activity and fall within the jurisdiction of the U.S. courts are enumerated. The third clause of subsection 1605(a)(2) follows:

[F]oreign state shall not be immune from the jurisdiction of a court of the United States in any case-in which the action takes place] outside the territory of the United States in connection with a commercial activity of the foreign state elsewhere and that act causes a direct effect in the United States;

It is obvious that the intent of Congress here is to allow private individuals--whether personal or corporate entities--to redress grievances suffered at the hands of a foreign sovereign while engaged in commerce.\(^3\) By applying the restrictive principle of sovereign immunity in a codified form there will be two positive effects: (1) commerce is enhanced by allowing private individuals to confidently proceed into commercial transactions with sovereigns knowing that they are not left without defense, and (2) impress upon sovereigns their responsibilities as trading partners.\(^4\) Before this concept can be applied however, it must be understood what constitutes a 'commercial act'. Briefly scanning the development of this term through history will allow for a more stable understanding of the present conceptions.

**Public and Private Acts**

The basis of the distinction between the types of acts a state can participate in comes from the French idea of public and private acts. While this distinction began within the French domestic judicial system, the French soon applied it to international cases and the theory spread rapidly.\(^5\)

In attempting to make the public and private dis-

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tinction, two different tests developed: 1) the nature test, and 2) the purpose test. The nature test reduces the issue to the nature of the act. In other words, if the act were something which could be performed by a private individual, the act would be a private act and not immune. This would apply to acts like entering into contracts and managing property, things that do not require the power of the state to perform. The purpose test on the other hand ignores the nature of the act and judges only the purpose of the act: why was the contract entered into? If it is determined that the contract was entered into for a public purpose—clothing the military for example—then that contractual act which the nature test would allow to be adjudicated would be immune under the purpose test.

The question of what test to apply to cases in U.S. courts spawned a dispute between the State Department and the courts; the State Department held to the nature test while the courts held to the purpose test. It was to settle disputes like this and help solidify the application of immunity that the FSIA was enacted. The FSIA gives the decision making power for such cases to the courts, but also holds that they must apply the nature test to questions of immunity.

A "commercial activity" means either a regular course of commercial conduct or a particular commercial transaction or act. The commercial character of an activity shall be determined by reference to the nature of the course of conduct or particular transaction or act, rather than by reference to its purpose.7

6 Ibid., p.231.

7 Public Law 94-583, ss 1603(d).
While it is clear that the nature test must be applied, another distinction must be made: was the act in question itself a commercial action, or was it a sovereign action committed through a commercial facade? This is a determination that usually must be made independent of the nature test. This distinction is brought out in Arango v. Guzman Travel Advisors Corp. 621 F.2d 1371. The court ruled that although Guzman was obviously involved in political activities, the specific act in question stemmed directly from their commercial activities in the United States and therefore, was not covered by sovereign immunity. Thus, it is not the nature of the entity, but the nature of the act that must be ruled on.

Establishing Direct Effects--Case Examples

With the nature test for a commercial activity established, there still remain numerous ambiguities. With the limitless number of possible cases, there is no feasible way to codify a perfect definition of commercial activity. Therefore, this penumbral area will have to be pronounced individually by each court to hear such a case, using the guidelines of the FSIA. Although not perfect, it appears that this is as close as the courts can come to erecting a uniform standard to solidify the commercial activity clause. With this in place, the focus needs to be shifted to perhaps the most problematic clause of 1605(a)(2): what constitutes "a direct effect in the United States?"

Through its case history, the direct effect clause has proven to be extremely fluid. There are, however, three common threads that can be seen when examining cases where the jurisdiction of the case has turned on this clause: 1) there must be certain minimum contacts between the acts of the sovereign in question and the United States, 2) the act’s effects in the Uni-
ted States must be foreseeable and the act must be engineered, and 3) the effects in question must be directly felt in the United States.

In order to illustrate these common points, four cases will be compared, with additional examples used when helpful. These cases are: 1) Texas Trading v. Federal Republic of Nigeria 647 F.2d 200 (1981), 2) Callejo v. Bancomer, S.A. 764 F.2d 1101 (1985), 3) Reale Interns, Inc. v. Federal Republic of Nigeria 562 F.Supp 56 (1983), and 4) East Europe Domestic International Sales Corp. v. Terra. 467 F.Supp 383 (1979). By looking at these cases and applying the three previously mentioned common threads, it is possible to gain some insight into the subtleties of the direct effects clause.

Rather than attempting to give the facts of each case as well as an explanation of the court’s action, attention will be focused on the common threads, with reference to the court’s action on each case as it applies.

First to be examined is the criteria for what constitutes minimum contacts. While the case which set the standard for minimum contacts was not dealing with immunity it did raise the question of the court’s jurisdiction. The same principle applies to immunity cases; the court must first establish jurisdiction and to make this determination in cases involving a sovereign as the defendant, the court must establish that there are indeed minimum contacts. A very loose reading of the above cases might suppose that direct financial effects could be considered sufficient to establish minimum contact. Upon closer examination, however, it is found that financial effects within the U.S. are not

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enough; in each case the financial effect must be linked to other contacts within the United States.

*Texas Trading*, a case that has been thought by some to be the first case to establish financial harm as sufficient minimum contact, can be seen to contain deeper commercial connections within the United States than the financial loss to the corporation.\(^9\) When determining their jurisdiction, the court made note of the harmed corporation being an American entity, but the court also noted that the method of payment was to be conducted through an American institution within the jurisdiction of the court. Thus, not only had an American entity been financially harmed, it had been harmed by a sovereign availing itself of American banking institutions.

This same principle can be seen in *Reale*. In many ways *Reale* mirrors *Texas Trading*, but one major difference is the location of the bank of payment. In *Reale*, payment was to be made through a Spanish bank. The minimum contacts were established by the Nigerian use of an American financial firm--Morgan--as a link in the chain of payment.

It is clear from the record testimony that, although the documents called for by the letter of credit could be presented to Banco de Bilbao, payment could be effected only by Morgan in New York, to whom Banco de Bilbao would be obliged to transmit the papers presented to obtain payment.

That being so, the case clearly falls within the FSIA, 28 U.S.C. subsection 1605 (a)(2) ... \(^10\)

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It would appear from the above that while the court’s interpretation of a direct effect has expanded to where financial loss is a definite factor, minimum contacts must still be established for the court to claim jurisdiction under the FSIA.

Likewise, in Callejo it appears that minimum contacts are again guiding the court. While there are grounds to assert that the commercial action taken by Bancomer may have actually taken place within the United States--shifting the issue from the third clause of 1605(a)(2) to the first clause of that same paragraph--the court denied this possibility and ruled on the direct effects clause. The court held that the breach of the certificates of deposit in question caused a direct effect within the United States, but this effect appears to be simply financial loss to an individual. The court, however, may have also used the concept of American banking activities to establish minimum contact within the United States, if not explicitly, at least implicitly.11

Callejo also makes the point that "the conduct must have a 'substantial' effect in the United States 'as a direct and foreseeable result of the conduct outside the territory.'"12 In other words, the courts recognize a difference between acts which are fortuitous and those which are engineered. In Callejo, the courts ruled that the direct effect of Bancomer’s action was foreseeable within the United States because of his extended business dealings with the Callejos.

Also in Reale, a connection was made between the action, cancelling payment, and its foreseeable effects within the United States. This almost appears to be

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12Ibid., p. 1111.
related to the concept of minimum contacts. Not only must the sovereign commit an action with direct effects in the United States, the effects of that action must be foreseeable, and therefore, the act engineered.\(^\text{13}\) This distinction protects the immunity of sovereigns when an attempt is made to hold them accountable for fortuitous wrongs. Also, in conjunction with fortuitous wrongs committed, the courts often hold that the act did not in fact produce a direct effect within the United States.\(^\text{14}\)

This brings up the last point: the criterion of a direct effect within the United States. This problem could easily be separated into two parts: what are the criteria for (1) a direct effect, and (2) in the United States.

One of the tests that the courts have applied to determine if the effect was direct is similar to a test applied in constitutional law: what was the intent of the framers? In the case of the FSIA, the courts have referred to the intent of Congress to allow the courts jurisdiction over certain types of cases.\(^\text{15}\) In each case, the courts have put forth the notion that they were ruling on the type of case Congress intended to remedy with the FSIA. The Second Circuit put it this way:

The question is, was the effect sufficiently "direct" and sufficiently "in the United States" that Congress would have wanted an American court to hear the case? No rigid parsing of ss 1605(a)(2) should lose sight of that purpose. We

\(^{13}\)Ibid.; Reale, p. 57.

\(^{14}\)Harris v. Intourist, Moscow 481 F.supp 1062 (1980).

\(^{15}\)Callego, p.1111; Reale, p. 57; Texas Trading, p. 311.
have no doubt that Congress intended to bring suits like these into American courts.\textsuperscript{16}

The courts also see a limit to this intent and recognize acts that produce indirect effects in the United States; in such cases, the courts protect the immunity of the sovereigns. Two examples examining corporate financial effects illustrate this trend.

In *East Europe Domestic International Sales Corp. v. Terra.*, 467 F.Supp 383, the court ruled that the immunity of Romania should be protected although the effects of the action—a cancelled contract—would obviously be felt in the United States.\textsuperscript{17} Two points illuminate the protection of immunity. First, the courts held that Terra. had not "projected itself" into the United States market to an extent that would allow jurisdiction; there were not minimum contacts established.\textsuperscript{18} When compared with *Texas Trading*, *East Europe* had lost potential profits from the cancellation of a contract rather than payment. The loss was only potential; they did not suffer a direct financial loss.

Another example of an indirect financial loss is found within *Carey v. National Oil Corp.*, 592 F.2d 673. National Oil Corp., a Libyan state owned firm, failed to deliver oil to a Bahamian subsidiary of an American corporation. The court held that although an American corporation suffered a financial loss, it was because of

\textsuperscript{16}Texas Trading, p. 313.


\textsuperscript{18}Ibid., p. 338.
an action that directly affected a Bahamian firm, and only secondarily affected the American parent corporation. Therefore, while it is obvious that there was a financial effect within the U.S., the court held that the effect was not directly within the U.S.

Conclusion

It is obvious that although Congress intended to codify a rule which would bring sovereigns and private entities into a more equal relationship in the marketplace, there remains an amorphous element to sovereign immunity in commercial matters. Two symptoms of this element remain: what are the criteria which must be met to establish (1) a commercial activity, and (2) a direct effect in the United States. As cases develop that fall into the penumbral areas of these exceptions, the courts have several avenues through which to reach their decision. One option traces the intent of Congress to see if it encompasses the case at bar. Another avenue goes back through the case history of the FSIA looking for common applications. Regardless of the avenue chosen--or more properly the mixtures of avenues--the application of the FSIA appears to have been fairly fluid in the past, and promises to remain so in the future.

Congress certainly did not enumerate each act that would be considered commercial, or which effects would be considered direct; to expect such an enumeration from either Congress or the courts is unreasonable. Congress did, however, enlighten their intended meaning of commercial activity, and the courts are applying three principles to cases which come before them: (1) there needs to be minimum contact with the act in question and the United States; (2) the effects must have been foreseeable and the act in question engineered, not fortuitous; and (3) the effects must be directly felt in the United States.
As long as the courts of the United States function under the present Constitution which allows judges to weigh the facts and pronounce their opinions, this is probably the greatest extent to which sovereign immunity can be codified. Although the individual remains at some risk in the marketplace, the FSIA increases the level of order and certainty found in the application of the principle of restrictive sovereign immunity.

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