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## COMMENT: *L'Europeenne de Banque v. La Republic de Venezuela*: Unnecessarily Permitting Foreign Plaintiffs to Sue Foreign Governments Under the Foreign Sovereign Immunities Act

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# COMMENTS

## ***L'EUROPEENNE DE BANQUE v. LA REPUBLIC DE VENEZUELA: UNNECESSARILY PERMITTING FOREIGN PLAINTIFFS TO SUE FOREIGN GOVERNMENTS UNDER THE FOREIGN SOVEREIGN IMMUNITIES ACT***

### I. INTRODUCTION

One result of the increased globalization of world trade has been an increase in litigation in which a foreign state is a defendant in a United States court.<sup>1</sup> To ensure that United States citizens and corporations have reliable access to judicial review of their disputes, Congress passed the Foreign Sovereign Immunities Act of 1976 (FSIA or Act).<sup>2</sup> Under the FSIA, claims of

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1. Note, *Suits by Foreigners Against Foreign States in United States Courts: A Selective Expansion of Jurisdiction*, 90 YALE L.J. 1861, 1862 (1981) [hereinafter Note, *Foreigner — Foreign State Suits*].

The legislative history of the Foreign Sovereign Immunities Act (FSIA or Act) indicates the variety of such transactions:

Instances of . . . [contact between American citizens and Foreign states] occur when [United States] businessmen sell goods to a foreign state trading company, and disputes may arise concerning the purchase price. Another [instance] is when an American property owner agrees to sell land to a real estate investor that turns out to be a foreign government entity and conditions in the contract of sale may become a subject of contention. Still another example occurs when a citizen crossing the street may be struck by an automobile owned by a foreign embassy.

*Id.* at n.7 (quoting H.R. REP. NO. 1487, 94th Cong., 2d Sess. 6-7, reprinted in 1976 U.S. CODE CONG. & ADMIN. NEWS 6604, 6605 [hereinafter H.R. REP. NO. 1487]).

2. Foreign Sovereign Immunities Act of 1976, Pub. L. No. 94-583, 90 Stat. 2892 (codified as amended at 28 U.S.C. §§ 1602-1611 (1988)).

The principle of foreign sovereign immunity has been defined as:

[A] rule of customary law rather than of mere comity, and it means that a foreign sovereign state, its public property and its official agents are in general immune from the local jurisdiction unless the foreign state consents to its exercise. If any question arises between the territorial sovereign and a foreign state

jurisdictional immunity are to be determined by federal and state courts in conformity with the principles set forth in the Act.<sup>3</sup> Although the Act's premise is that foreign governments have jurisdictional immunity from United States courts, there are five exceptions to this immunity, one of which is the "commercial activities exception." If the foreign sovereign's activity in question is deemed to be commercial, one of three additional factors must be present in order to subject the foreign sovereign to the jurisdiction of United States courts.<sup>4</sup> One such factor is that the activity of the foreign sovereign must have a direct effect in the United States.<sup>5</sup>

In *L'Europeenne de Banque v. La Republic de Venezuela*,<sup>6</sup> the United States District Court for the Southern District of New York was asked to determine whether the Venezuelan Government's nationalization of a Venezuelan bank fell within the commercial activities exception of the FSIA, and, if it did, whether the financial injury that resulted to a consortium of foreign banks that had loaned money to the Venezuelan bank had a direct effect in the United States.<sup>7</sup> The court ultimately dismissed the suit because it did not have personal jurisdiction over the Venezuelan Government.<sup>8</sup> Before doing so, however, it held that subject matter jurisdiction existed under the FSIA because the nationalization constituted commercial activity within the meaning of the Act and the nationalization had a direct effect in the United States.<sup>9</sup>

Commentators have often criticized the FSIA for its vague definitions of such important terms as "commercial activity," and have also criticized United States courts for failing to de-

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it can only be taken up through the diplomatic channel or in some international forum unless the foreign state waives its immunity from the local jurisdiction.

J. BRIERLY, *THE LAW OF NATIONS* 243-44 (6th ed. 1963).

3. 28 U.S.C. § 1602 (1988).

4. Under the FSIA, a foreign state is not immune from United States jurisdiction when an action against it is based upon: (1) a commercial activity conducted in the United States by that state; (2) an act performed in the United States in connection with a commercial activity of that state elsewhere; or (3) an act outside the United States in connection with a commercial activity of the foreign state carried on elsewhere that causes a direct effect on United States commerce. *Id.* at § 1605.

5. *Id.*

6. 700 F. Supp. 114 (S.D.N.Y. 1988).

7. *L'Europeenne*, 700 F. Supp. at 114.

8. *Id.* at 125.

9. *L'Europeenne*, 700 F. Supp. at 119, 121.

velop a consistent framework for determining when an act by a foreign sovereign constitutes commercial activity.<sup>10</sup> In contrast, United States courts have consistently construed the direct effect exception strictly. This Comment examines the case law and legislative history of the commercial activities exception of the FSIA, the "direct effect" language of the exception, and the court's decision in *L'Europeenne*. It concludes that the court's ruling in *L'Europeenne* reflects the inconsistency often present in deciding the commercial activity question. Further, this Comment concludes that the court's ruling contravenes Congressional intent as well as the line of cases regarding what constitutes a direct effect under the Act. The court's holding unnecessarily expands the definitions of both commercial activity and direct effect.

This Comment will argue that courts should return to the original model of the restrictive theory of foreign sovereign immunity when determining whether the acts of a foreign sovereign should be considered commercial within the meaning of the FSIA.<sup>11</sup> The courts should determine whether the act could have been carried out by a private individual or if the act was purely governmental, which would entitle it to sovereign immunity. This was the earliest embodiment of the restrictive theory and is the standard the Act's legislative history indicates Congress intended when the FSIA was passed.<sup>12</sup>

In determining whether an act of a foreign sovereign has a direct effect in the United States, courts should strictly adhere to the language of the Act, which refers to Section 18 of the Restatement (Second) of Foreign Relations Law (Section 18).<sup>13</sup> Section 18 calls for a substantial, direct, and foreseeable effect in the United States of the conduct abroad.<sup>14</sup>

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10. Lauterpacht, *The Problem of Jurisdictional Immunities of Foreign States*, 28 BRIT. Y.B. INT'L L. 220, 222-24 (1951). See also *infra* notes 21-51 and accompanying text. Comment, *Martin v. Republic of South Africa: Alienating Injured Americans*, 15 BROOKLYN J. INT'L L. 153, 154-55 (1989) [hereinafter Comment, *Martin v. South Africa*]. Comment, *De Sanchez v. Banco Central De Nicaragua: Too Many Exceptions to the Commercial Activities Exception of the Foreign Sovereign Immunities Act of 1976?*, 14 BROOKLYN J. INT'L L. 715, 719 (1988) [hereinafter Comment, *De Sanchez v. Nicaragua*].

11. For a discussion of the restrictive theory, see Comment, *De Sanchez v. Nicaragua*, *supra* note 10, at 719-22.

12. H.R. REP. NO. 1487, *supra* note 1, at 7, reprinted in 1976 U.S. CODE CONG. & ADMIN. NEWS at 6605. Comment, *De Sanchez v. Nicaragua*, *supra* note 10, at 720.

13. RESTATEMENT (SECOND) OF FOREIGN RELATIONS LAW § 18 (1965) [hereinafter RESTATEMENT (SECOND)].

14. RESTATEMENT (SECOND), *supra* note 13, at § 18. See *infra* note 55.

This Comment concludes that although providing a forum for the resolution of disputes might occasionally promote United States interests, the adjudication of claims by foreign plaintiffs against foreign sovereigns by United States courts could lead to the avoidance of the United States as a place to do business and also might hurt American foreign policy interests.

## II. BACKGROUND

Congress enacted the FSIA to regularize the law governing foreign sovereign immunity and to make it less dependent on political factors.<sup>15</sup> Congress also intended that the Act provide the "sole and exclusive standards to be used in resolving questions of sovereign immunity."<sup>16</sup> To ensure consistent treatment of foreign governments in United States courts, the Act places the determination of sovereign immunity exclusively in the hands of the courts.<sup>17</sup> The FSIA codifies the restrictive theory of

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15. Until 1952 foreign nations enjoyed absolute immunity from the judicial process of the United States. This policy was first referred to in *Schooner Exchange v. M'Faddon*, 11 U.S. (7 Cranch) 116, 146 (1812) (granting immunity to French Warship within United States territorial waters). By the twentieth century, the Supreme Court had formally adopted the policy that separation of powers required judicial deference to the Executive in matters concerning foreign sovereign immunity. The decision to recognize or disregard the state's immunity came to rest with the United States Department of State (State Department), which made formal suggestions to the courts regarding immunity. See, e.g., *Republic of Mexico v. Hoffman*, 324 U.S. 30, 34-36 (1945) ("the policy recognized both by the Department of State and the Court [is] that the national interest will be best served when controversies growing out of the judicial seizure of vessels of foreign governments are adjudicated through diplomatic channels rather than by the compulsion of judicial proceedings"). These recommendations bound the courts after *Ex parte Peru*, 318 U.S. 578, 588 (1943) (suit dismissed because of State Department determination of immunity).

As states assumed a greater role in commercial trade, however, the absolute immunity of foreign states was challenged under the theory that there was no justification under modern international law principles for allowing foreign states to avoid all liability arising from their commercial activities or torts. In 1952 the State Department responded to these criticisms by adopting the restrictive theory of immunity, which limits immunity to public, as opposed to commercial, acts of the foreign sovereign. Letter of Acting Legal Adviser, Jack B. Tate, to acting Attorney General Philip B. Perlman (May 19, 1952) reprinted in 26 DEP'T ST. BULL. 984 (1952) [hereinafter Tate Letter]. The State Department's position remained dispositive until 1977, when the FSIA's delegation of decision making authority to courts took effect.

For a fuller account of the history of the doctrine of foreign sovereign immunity, see, e.g., Comment, *De Sanchez v. Nicaragua*, *supra* note 10; Comment, *Martin v. South Africa*, *supra* note 10.

16. H.R. REP. NO. 1487, *supra* note 1, at 12, reprinted in 1976 U.S. CODE CONG. & ADMIN. NEWS at 6610.

17. H.R. REP. NO. 1487, *supra* note 1, at 12, reprinted in 1976 U.S. CODE CONG. & ADMIN. NEWS at 6610.

sovereign immunity.<sup>18</sup> It grants blanket immunity to foreign governments but enumerates five exceptions and conditions under which a foreign sovereign will be subject to the jurisdiction of United States courts.<sup>19</sup> One of these five exceptions is the commercial activities exception, which is designed to cover certain activities carried on within or outside the territorial jurisdiction of the United States.<sup>20</sup>

#### *A. The Commercial Activities Exception to the Foreign Sovereign Immunities Act*

The commercial activities exception<sup>21</sup> is the most litigated, and therefore the most important, exception to sovereign immunity created by the Act.<sup>22</sup> Under the Act, commercial activity is

The FSIA also provides standards for determining if personal jurisdiction over a foreign defendant exists and restricts the immunity of foreign government property from satisfaction of judgments. *Id.* at 16, *reprinted in* 1976 U.S. CODE CONG. & ADMIN. NEWS at 6610-12.

18. 28 U.S.C. §§ 1605, 1607 (1988).

19. The five exceptions are: (1) waiver of sovereign immunity by the foreign government; (2) commercial activity by the foreign government in the United States; (3) conversion of property in violation of international law; (4) disputes over real property located in the United States; and (5) noncommercial tortious acts. 28 U.S.C. § 1605(a)(1)-(5) (1988).

The Act applies only to foreign states, their political subdivisions, and their agencies and instrumentalities. *Id.* at § 1603(a). This section defines "foreign state" for all sections of the Act except section 1608. For section 1608 purposes, "foreign state" refers only to the state itself. *Id.* at § 1608.

An agency or instrumentality is defined as any entity:

- (1) which is a separate legal person, corporate or otherwise, and
- (2) which is an organ of a foreign state or political subdivision thereof, or a majority of whose shares or other ownership interest is owned by a foreign state or political subdivision thereof, and
- (3) which is neither a citizen of a state of the United States as defined in section 1332(c) and (d) of this title, nor created under the laws of any third country.

*Id.* at § 1603.

20. *Id.* at § 1605(a)(2).

21. The commercial activities exception provides in pertinent part:

(a) A foreign state shall not be immune from the jurisdiction of courts of the United States or of the [s]tates in any case —

(2) in which the action is based upon a commercial activity carried on in the United States by the foreign state; or upon an act performed in the United States in connection with a commercial activity of the foreign state elsewhere; or upon an act 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 . . .

*Id.*

22. H.R. REP. NO. 1487, *supra* note 1, at 18-19, *reprinted in* 1976 U.S. CODE CONG. & ADMIN. NEWS at 6617. See also Note, *Foreigner — Foreign State Suits*, *supra* note 1,

defined as "either a regular course of commercial conduct or a particular commercial transaction or act."<sup>23</sup> The Act also states that "the commercial character [of a foreign state's conduct] 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."<sup>24</sup> However, it is not sufficient that the foreign state engages in commercial activity; the claim must be related to the specific commercial activity or act upon which jurisdiction is based.<sup>25</sup> Fear of transforming United States courts into international courts of claims and of adversely affecting international trade were motivating factors underlying the related claim requirement.<sup>26</sup> Despite this limitation, it was argued shortly after the Act's passage that the Act's effect would be to increase the number of suits filed in United States courts.<sup>27</sup>

Entities that usually engage in an activity for profit are presumed to be engaged in a commercial activity.<sup>28</sup> Because the definition is so ambiguous, however, courts have had difficulty in determining whether the activities of foreign sovereigns constitute commercial activity, and courts have noted the FSIA's lack of clarity.<sup>29</sup>

The leading case in this area is *Texas Trading & Milling Corp. v. Federal Republic of Nigeria*.<sup>30</sup> In *Texas Trading*, Nigeria contracted to buy huge quantities of cement from several trading companies, including Texas Trading & Milling, a New

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at 1865 n.25. See also Dellapenna, *Suing Foreign Governments and their Corporations: Sovereign Immunity*, 85 Com. L.J. 228, 230 (1980) (describing the commercial activities exception as the "core" of the FSIA).

23. 28 U.S.C. § 1603(d) (1988).

24. *Id.*

25. *Id.*

26. *Verlinden B.V. v. Central Bank of Nigeria*, 461 U.S. 480, 490 (1983) (quoting the testimony of Bruno A. Ristau, Hearings on H.R. 11315, at 315).

Examples of commercial activities provided in the Act's legislative history include "a foreign government's sale of a service or product, its leasing of property, its borrowing of money, its employment or engagement of laborers, clerical staff or public relations or marketing agents, or its investment in a security of an American corporation, would be among those included within the definition." See H.R. REP. NO. 1487, *supra* note 1, at 16, reprinted in 1976 U.S. CODE CONG. & ADMIN. NEWS at 6615.

27. Note, *Foreigner — Foreign State Suits*, *supra* note 1, at 1862.

28. H.R. REP. NO. 1487, *supra* note 1, at 16, reprinted in 1976 U.S. CODE CONG. & ADMIN. NEWS at 6615.

29. *Texas Trading & Milling Corp. v. Federal Republic of Nigeria*, 647 F.2d 300, 308 (2d Cir. 1981), *cert. denied*, 454 U.S. 1148 (1982).

30. *Id.*

York corporation.<sup>31</sup> Nigeria repudiated its contracts when it found that its ports could not handle all the goods being imported.<sup>32</sup> The trading companies sued for breach of contract.<sup>33</sup> Nigeria sought a declaration of sovereign immunity.<sup>34</sup> The Court of Appeals for the Second Circuit (Second Circuit) held that Nigeria's act of entering into contracts to buy cement was commercial within the meaning of the FSIA.<sup>35</sup> The Second Circuit set forth three possible standards for determining if a foreign sovereign's conduct constituted commercial activity. The most important of the three was derived from the legislative history of the FSIA: the court concluded that if the activity was one in which a private person could engage, it was commercial, and under the Act, a lawsuit based on that activity could be heard in the United States.<sup>36</sup> The court dismissed Nigeria's argument that

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31. *Id.* at 303. Trading companies are not industrial corporations. They buy products from one party and sell to another, hoping to make a profit on the differential. Although it had the money to pay for all the goods it was buying, Nigeria's ports could not handle the deluge of imports. *Id.*

32. *Id.* at 302.

33. *Id.* Four New York trading companies sued. Texas Trading lost its suit when the judge found jurisdiction lacking. *Texas Trading & Milling Corp. v. Federal Republic of Nigeria*, 500 F. Supp. 320 (S.D.N.Y. 1980). The other three companies, in a consolidated action, were awarded \$1.857 million after the trial judge found jurisdiction present. *Decor by Nickkei Int'l v. Federal Republic of Nigeria*, 497 F. Supp. 893 (S.D.N.Y. 1980). The two cases were consolidated in *Texas Trading*, 647 F.2d at 300.

34. *Texas Trading*, 647 F.2d at 302.

35. *Id.* at 310.

36. *Id.* at 309. The court relied on the statement of a high Justice Department official to support its conclusion: "[I]f a government enters into a contract to purchase goods and services, that is considered a commercial activity. It avails itself of the ordinary contract machinery. It bargains and negotiates. It accepts an offer. It enters into a written contract and the contract is to be performed." Statement of Bruno Ristau, then chief of the Foreign Litigation Section of the Civil Division, Department of Justice. *Id.* (quoting 1976 *Hearings* at 51).

The second standard the court cited was "the very large body of case law which exist[ed]" in American law upon passage of the Act. *Id.* (quoting testimony of Monroe Leigh, 1976 *Hearings* at 53). The court went on to cite a series of cases which held that, since the Tate Letter, *see supra* note 15, United States courts had followed the restrictive theory of jurisdiction. *Texas Trading*, 647 F.2d at 309 (quoting testimony of Charles N. Bower, then Legal Adviser of the Department of State, 1973 *Hearings* at 15). (The cases the court cited included *Petrol Shipping Corp. v. Kingdom of Greece*, 360 F.2d 103 (2d Cir. 1965), *cert. denied*, 385 U.S. 931 (1966); *Victory Transp., Inc. v. Comisaria General de Abastecimiento y Transportes*, 336 F.2d 354 (2d Cir. 1964), *cert. denied*, 381 U.S. 934 (1965)).

The third standard was that of contemporary international law. The court found that the drafters of the FSIA intended to bring American sovereign immunity practices into line with that of other nations. *Texas Trading*, 647 F.2d at 309. The court found that international law follows the restrictive theory of immunity and that this, therefore, is what the drafters intended of United States law. *Id.* at 310 (citing State Immunity



the purpose for which the cement was to be used was not commercial.<sup>37</sup> The court stated that "if a government goes into the market places of the world and buys boots or cement — as a commercial transaction — that government should be subject to all the rules of the marketplace."<sup>38</sup>

Although many courts have followed the standard defining commercial activity described in *Texas Trading*, the definition of commercial activity employed by the Act has often lead to divergent results in cases with similar fact patterns. For example, in *Callejo v. Bancomer, S.A.*,<sup>39</sup> the plaintiffs were United States citizens who bought dollar-denominated certificates of deposit (CDs) from a privately owned Mexican bank.<sup>40</sup> In 1982 Mexico nationalized all privately owned banks, including Bancomer, and promulgated regulations requiring that banks pay interest and principal on the CDs in Mexican Pesos at the official rate of exchange, a considerably lower amount of money than Bancomer's contract with the plaintiffs provided. The plaintiffs brought suit for breach of contract and securities violations.<sup>41</sup>

The Court of Appeals for the Fifth Circuit (Fifth Circuit) held that once Bancomer was nationalized by the Mexican Government it became an agency of a foreign state within the meaning of the FSIA and would ordinarily be entitled to immunity from jurisdiction of United States courts under the FSIA.<sup>42</sup> The court held, however, that the suit arose from Bancomer's commercial activity.<sup>43</sup> It stated that "analysis must focus on the defendant's acts which are the basis of the action and not on the separate acts of other sovereign instrumentalities or agencies."<sup>44</sup> The court stated that the gravamen of the complaint was the

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Act, 1978 § 3 (United Kingdom); Council of Europe, European Convention on State Immunity art. 4 (1972), reprinted in 1976 *Hearings* at 37, 38; 45 I.L.R. 57 (1963) (West Germany)).

37. *Texas Trading*, 647 F.2d at 310.

38. *Id.* (quoting *Trendtex Trading Corp. v. Central Bank of Nigeria*, [1977] 2 W.L.R. 356, 369, 1 ALL E.R. 881). For a discussion of whether Nigeria's repudiation had a direct effect in the United States within the meaning of the FSIA, see *infra* notes 58-62 and accompanying text.

39. 764 F.2d 1101 (5th Cir. 1985).

40. *Callejo*, 764 F.2d at 1106.

41. *Id.* at 1104.

42. *Id.* at 1106.

43. *Id.* at 1107.

44. *Id.* at 1108 (quoting *Braka v. Bancomer, S.A.*, 589 F. Supp. 1465, 1469 (S.D.N.Y. 1984)).

sale of the CDs and therefore the commercial activities exception applied. Relying on *Texas Trading*, the court held that it was irrelevant that it was the Mexican Government's decrees that required Bancomer to breach the contract.<sup>45</sup>

*Callejo* was distinguished, however, in *De Sanchez v. Banco Central de Nicaragua*.<sup>46</sup> In *De Sanchez*, the Fifth Circuit held that the Nicaraguan Central Bank's refusal to honor a check on the country's foreign exchange reserves did not constitute commercial activity.<sup>47</sup> The *De Sanchez* court distinguished *Callejo* by noting that Banco Central "did not enter the marketplace as a commercial actor" but became involved in the transaction solely because of its role in regulating sales of foreign exchange.<sup>48</sup> Because currency exchange regulation is a sovereign function in which a private party cannot engage, the court held that the commercial activities exception did not apply.<sup>49</sup>

The FSIA's ambiguous definition of commercial activity has lead to confusion as to when acts of foreign sovereigns will subject them to the jurisdiction of United States courts. This problem can be resolved by returning to the original definition of restrictive immunity. Courts should distinguish between purely governmental acts and acts of a sovereign that a private citizen or corporation could also carry out, such as purchasing consumer goods in the international marketplace.<sup>50</sup> Although this standard has been criticized as too difficult to apply, factors such as the presence or absence of a profit motive can be developed by courts to determine whether or not the activity is commercial.<sup>51</sup>

### B. *The Direct Effect Clause*

The commercial activities exception confers jurisdiction on United States courts for three types of activities.<sup>52</sup> One of these three is an act by a foreign sovereign outside the United States that causes a direct effect in the United States.<sup>53</sup> Although Con-

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45. *Id.* at 1109.

46. 770 F.2d 1385, 1391 (5th Cir. 1985).

47. *De Sanchez*, 770 F.2d at 1393.

48. *Id.*

49. *Id.* at 1393-94.

50. See *infra* note 107 and accompanying text.

51. See, e.g., *Letelier v. Republic of Chile*, 748 F.2d 790, 797 (2d Cir. 1984), cert. denied, 471 U.S. 1125 (1985). See *infra* notes 108-11; see also *MOL, Inc. v. People's Republic of Bangladesh*, 736 F.2d 1326, 1328-29 (9th Cir. 1984). See *infra* notes 112-14.

52. 28 U.S.C. § 1605 (1988). See *supra* note 4.

53. 28 U.S.C. § 1605(a)(2) (1988).

gress did not define direct effect in the FSIA, it did state that where commercial conduct abroad causes a direct effect in the United States, courts should exercise jurisdiction consistently with the principles espoused in Section 18.<sup>54</sup> Section 18 states in part that the effects of the foreign conduct in the United States must be substantial, direct, and foreseeable.<sup>55</sup> The legislative history of the Act indicates that Congress was concerned with the possibility that courts would be forced to hear many more cases than they had prior to the Act's passage.<sup>56</sup> Therefore, courts should apply the direct effect clause strictly. Courts have generally done this, and plaintiffs have had to overcome a high hurdle to prove that the foreign sovereign's act that caused their injury also had a direct effect in the United States.<sup>57</sup>

Courts are likely to find a direct effect where a financial injury is suffered by a United States corporation because of a foreign sovereign's act outside the United States. In *Texas Trading*, the court, having found that Nigeria had engaged in commercial activity, addressed the issue of whether that activity

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54. H.R. REP. NO. 1487, *supra* note 1, at 19, reprinted in 1976 U.S. CODE CONG. & ADMIN. NEWS at 6618. RESTATEMENT (SECOND), *supra* note 13, at § 18.

55. Section 18 provides:

A state has jurisdiction to prescribe a rule of law attaching legal consequences to conduct that occurs outside its territory and causes an effect within its territory, if either

(a) the conduct and its effect are generally recognized as constituent elements of a crime or tort under the law of states that have reasonably developed legal systems, or,

(b) (i) the conduct and its effect are constituent elements of activity to which the rule applies;

(ii) the effect with the territory is *substantial*;

(iii) it occurs as a *direct and foreseeable* result of the conduct outside the territory; and

(iv) the rule is not inconsistent with the principles of justice generally recognized by states that have reasonably developed legal systems.

RESTATEMENT (SECOND), *supra* note 13, at § 18 (emphasis added). See *Maritime Int'l Nominees Establishment v. Republic of Guinea*, 693 F.2d 1094, 1110 (D.C. Cir. 1982).

56. Note, *Foreigner — Foreign State Suits*, *supra* note 1, at 1862.

57. Effects jurisdiction derives from a state's interest in protecting those within its borders and in governing events within its borders. Thus, to determine whether a corporation has sustained a direct effect within the United States, a court must determine whether the corporation has sufficiently manifested itself within the jurisdiction so that the loss sustained by the corporation may be deemed to have been sustained by an entity within the jurisdiction. Note, *Effects Jurisdiction under the Foreign Sovereign Immunities Act and the Due Process Clause*, 55 N.Y.U. L. REV. 474, 512 (1980) [hereinafter Note, *Effects Jurisdiction*].

had a direct effect in the United States.<sup>58</sup> It held that "the relevant inquiry under the direct effect clause when the plaintiff is a corporation is whether the corporation has suffered a direct financial loss."<sup>59</sup> Although it conceded that neither the term "direct" nor "effect" was easy to define, the court ruled that since the plaintiff was a United States corporation that was to be paid in the United States, Nigeria's repudiation created a direct effect in the United States.<sup>60</sup> The fact that Texas Trading was a United States corporation was central to the court's ruling.<sup>61</sup> Indeed, the court noted that the question of whether a failure to pay a foreign corporation in the United States or a failure to pay a United States corporation abroad creates an effect in the United States was not before it.<sup>62</sup>

In a case where a foreign plaintiff sued a foreign sovereign, *Maritime Int'l Nominees Establishment (MINE) v. Republic of Guinea*,<sup>63</sup> the court refused to find a direct effect in the United States when Guinea's breach of contract resulted in lost profits to a third party United States corporation.<sup>64</sup> In *MINE*, the plaintiff was a Liechtenstein corporation which entered into a contract with the Guinean Government to establish and provide shipping services to transport Guinean bauxite to foreign markets.<sup>65</sup> *MINE* filed suit in the District of Columbia to enforce an arbitrator's ruling, which Guinea opposed on the grounds of sovereign immunity.<sup>66</sup> *MINE* argued that Guinea's breach had a direct effect in the United States because of profits lost by the United States corporation that was "closely allied with *MINE*" and that was financially harmed by the breach.<sup>67</sup> The *MINE* court rejected this argument and found that Guinea was immune under the FSIA because, even if *MINE*'s allegations of harm to the United States corporation were true, it did not constitute a direct effect in the United States as contemplated by

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58. *Texas Trading & Milling Corp. v. Federal Republic of Nigeria*, 647 F.2d 300, 311-12 (2d Cir. 1981).

59. *Texas Trading*, 647 F.2d at 312.

60. *Id.*

61. *Id.*

62. *Id.*

63. 693 F.2d 1094 (D.D.C. 1982).

64. *MINE*, 693 F.2d at 1111.

65. *Id.* at 1095.

66. *Id.* at 1097-98.

67. *Id.* at 1110.

the Act.<sup>68</sup> The court reasoned that the harm alleged was not sufficiently direct and foreseeable, since the corporation's involvement in the venture was not reasonably contemplated by the contract between MINE and Guinea.<sup>69</sup>

Another recent case involving the direct effect clause is *Gould, Inc. v. Pechiney Ugine Kuhlmann*.<sup>70</sup> In *Gould*, an American corporation brought action alleging violation of the Racketeer Influence and Corrupt Organizations Act and misappropriation of trade secrets against a French corporation whose sole shareholder was the French Government.<sup>71</sup> The complaint alleged that the defendant bought trade secrets from a former employee of the plaintiff's and in doing so engaged in unfair competition.<sup>72</sup> The court, citing *Callejo*, found that the defendant's negotiations with the plaintiff's former employee constituted commercial activity.<sup>73</sup> The court went on to state that:

economic injury to a United States corporation, as a result of a foreign state's commercial activity may satisfy the 'direct effects' clause . . . if the corporation is the primary direct, rather than indirect, victim of the conduct, and if injurious and significant the financial consequences to that corporation were the foreseeable, rather than fortuitous, result of the conduct.<sup>74</sup>

The defendant argued that there was no direct effect in the United States because any financial loss the plaintiff would suffer would be due to competition in foreign markets.<sup>75</sup> The court rejected this contention, pointing out that plaintiff also alleged misappropriation of its trade secrets, and stating that "it is difficult to imagine conduct which will have a more direct effect upon plaintiff, which is located and operates in the United States."<sup>76</sup>

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68. *Id.*

69. *Id.* at 1110-11.

70. 853 F.2d 445 (6th Cir. 1988).

71. *Gould*, 853 F.2d at 447.

72. *Id.* at 447-48. The complaint also alleged that the defendant interfered with the plaintiff's relationship with its former employee, unlawfully appropriated plaintiff's proprietary information and trade secrets, and became unjustly enriched due to the misappropriation. *Id.* at 447.

73. The court stated "[a]n activity is commercial if it 'is of a type that a private person would customarily engage in for profit.'" *Id.* at 452 (quoting *Callejo v. Bancomer, S.A.*, 764 F.2d 1101, 1108 (5th Cir. 1985)). See *supra* notes 39-45.

74. *Gould*, 853 F.2d at 453.

75. *Id.*

76. *Id.*

United States courts have consistently applied the same test to determine whether the foreign sovereign's commercial activity has a direct effect in the United States. Relying on the legislative history's reference to Section 18, courts have strictly enforced the requirement that the financial injury must occur in the United States, and that it must be substantial, direct, and foreseeable.

### III. *L'EUROPEENNE DE BANQUE V. LA REPUBLIC DE VENEZUELA*

#### A. *Facts*

In November 1981 the plaintiffs, a consortium of foreign banks<sup>77</sup> lead by L'Europeenne de Banque (LEB), a bank incorporated in France, entered into a deposit lending agreement with Sociedad Financiera de Comercio (SFC), which, with its parent corporation, formed one of Venezuela's largest financial institutions. The deposit agreement had no termination date; in effect it provided SFC with \$30 million in revolving credit.<sup>78</sup> SFC was to repay the loan by depositing money in LEB's account in New York.<sup>79</sup> This, together with the fact that the loan was made and payable in United States dollars, was the only connection between the loan agreement and the United States.<sup>80</sup>

In reaction to concerns about the bank's financial safety, Venezuela took over the operations of SFC's parent corporation,

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77. The consortium included 14 foreign banks. Between the time the consortium was formed and the suit was filed, however, two other banks substituted for two original members. One of the two new banks was a United States bank, Norwest Bank Minneapolis, N.A. (Norwest), but the court discounted Norwest's presence in the consortium, holding that it was unclear whether it had joined before or after the repudiation had occurred. *L'Europeenne de Banque v. La Republic de Venezuela*, 700 F. Supp. 114, 116, 121 (S.D.N.Y. 1988).

78. *Id.* at 116.

79. *Id.* at 122.

80. *Id.* at 122, 125. According to L'Europeenne de Banque's (LEB) complaint, beginning in or before March 1982, defendant Juan Vincente Perez Sandoval, who then controlled Sociedad Financiera de Comercio (SFC) either directly or indirectly through intermediary corporations, embarked on a scheme to loot the assets of SFC and to defraud its creditors. The scheme did not come to the consortium's attention until March 1984 when SFC failed to make a payment due under the agreement. LEB, representing the consortium, met with SFC's officers, including Perez Sandoval, who persuaded LEB not to declare the loan in default. According to the complaint, Perez Sandoval subsequently made a series of false and misleading representations, including one for the provision of a collateral package (the assets a borrower pledges as security for a loan) as security for SFC's debts, which induced LEB to continue to forgo recourse to judicial remedies. Subsequently, Perez Sandoval fled Venezuela in 1985. *Id.* at 116.

SFC, and two affiliated credit organizations on June 30, 1985.<sup>81</sup> The resolution declaring the "intervention" granted all management powers to Venezuela's Deposit Guaranty and Bank Protection Fund (the Fondo).<sup>82</sup> The Fondo operated SFC for approximately fourteen months. On July 29, 1986, having already provided SFC with \$452 million in financial assistance, Venezuela revoked the authorizations to function of both SFC and its parent and ordered their immediate liquidations.<sup>83</sup> The consortium, unsecured and unpaid, responded by filing suit against the Venezuelan Government in United States District Court for the Southern District of New York.<sup>84</sup> Jurisdiction was alleged to be present under the FSIA.<sup>85</sup>

### B. Holding

The court first addressed the question of whether it possessed subject matter jurisdiction over the action.<sup>86</sup> It agreed with LEB that Venezuela had engaged in commercial activity within the meaning of the FSIA by intervening in SFC's affairs.<sup>87</sup> In support of this conclusion, the court relied on a case

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81. *Id.* at 117.

82. *Id.* La Republic de Venezuela's motion to dismiss stated that the Fondo is the Venezuelan equivalent to the Federal Home Loan Bank Board. *Id.* at 119 (quoting Memorandum of Defendant La Republic de Venezuela in Support of Motion to Dismiss at 19-21).

83. *Id.* at 117.

84. *Id.* The other defendants were SFC, its wholly-owned subsidiary, the vice-president of the Fondo who had run SFC between Venezuela's intervention and SFC's liquidation, and SFC's original management, who the complaint accused of plundering SFC's assets. See complaint paras. 2-9.

85. *L'Europeenne de Banque v. La Republic de Venezuela*, 700 F. Supp. 114, 117 (S.D.N.Y. 1988).

86. *Id.* (citing *Gross v. Houghland*, 712 F.2d 1034, 1036 (6th Cir. 1983), *cert. denied*, 465 U.S. 1025 (1984) ("federal court must satisfy itself that it has subject matter jurisdiction over the dispute before it addresses the merits of the claims")).

The court first held that neither the waiver nor the expropriation exceptions to the FSIA were applicable. LEB argued that, of the five exceptions to sovereign immunity provided by section 1605(a), three applied: waiver of sovereign immunity, commercial activity, and expropriation of assets in violation of international law. 28 U.S.C. §§ 1605 (a)(1)-(3) (1988).

87. *L'Europeenne de Banque*, 700 F. Supp. at 119. In response to LEB's argument that Venezuela had engaged in a de facto nationalization by intervening in SFC's financial affairs, the court pointed out that, although the term "intervention" has been equated with "nationalization," *id.* (citing *Menendez v. Saks & Co.*, 485 F.2d 1355, 1360 (2d Cir. 1973), *rev'd on other grounds sub nom*, *Alfred Dunhill of London, Inc. v. Republic of Cuba*, 425 U.S. 682 (1976); *Tabacalera Cubana, S.A. v. Faber, Coe & Gregg, Inc.*, 379 F. Supp. 772, 773-74 (S.D.N.Y. 1974)), "nationalization" implies permanency and profit motive. The court ruled that neither existed in this case. *Id.*

decided in 1927, *Metropolitan Savings Bank & Trust Co. v. Farmers' State Bank*,<sup>88</sup> which held that a bank which had been temporarily taken over by the state of Nebraska was not entitled to immunity from suit.<sup>89</sup>

Once the *L'Europeenne* court determined that the act of the Venezuelan Government constituted commercial activity, the next issue to be determined was whether that activity had a direct effect in the United States.<sup>90</sup> If it did, Venezuela's application for immunity would be rejected.<sup>91</sup> In determining whether this jurisdictional basis applied, the court held that nonpayment of a debt payable in the United States causes a direct effect in the United States, even when neither party is a United States citizen.<sup>92</sup> In support of this conclusion, the court first pointed to the Supreme Court's ruling in *Verlinden B.V. v. Central Bank of Nigeria*<sup>93</sup> as allowing such suits.<sup>94</sup> The *L'Europeenne* court conceded, however, that the *Verlinden* opinion held only that foreign plaintiffs could bring suit under FSIA if the substantive requirements of the Act are met.<sup>95</sup> The court further noted that *Verlinden* expressed no view as to whether the nonpayment of a

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88. 20 F.2d 775 (8th Cir. 1927), *cert. denied*, 276 U.S. 624 (1928). For a discussion of *Metropolitan Savings*, see *infra* notes 104-06 and accompanying text.

89. *Metropolitan Savings*, 20 F.2d at 779.

90. 28 U.S.C. § 1605(a)(2) (1988). In its brief supporting the motion to dismiss, Venezuela argued that, since only a sovereign could take over a bank, its intervention could not be seen as a commercial act, and therefore it did not need to reach the question of direct effect. Memorandum of Defendant La Republica de Venezuela in Support of Motion to Dismiss, 17-21.

91. LEB argued that Venezuela's intervention in SFC's financial affairs satisfied all three of the requirements of the FSIA. Venezuela was so certain that its intervention did not constitute commercial activity that its motion to dismiss did not make alternative arguments as to whether its behavior, even if found to be within the commercial activities exception, was entitled to immunity under the Act. The court first rejected LEB's claim that since Venezuela had assumed management of SFC it had also assumed oversight and management of the operations of SFC's subsidiaries, the three New York corporations also named as defendants. Since the corporations principal purpose was the management of real estate, the court stated, Venezuela's failure to repay the certificates of deposit was not "based upon the commercial activity carried on in the United States" as required by the Act. *L'Europeenne de Banque v. La Republic de Venezuela*, 700 F. Supp. 114, 120 (S.D.N.Y. 1988).

The second basis for jurisdiction under the FSIA, that the act was performed in the United States, did not apply, the court stated, since Venezuela's repudiation occurred in Venezuela. *Id.* at 121.

92. *Id.*

93. 461 U.S. 480 (1983). For a further discussion of *Verlinden*, see *infra* notes 120-32.

94. *L'Europeenne de Banque*, 700 F. Supp. at 121.

95. *Verlinden*, 461 U.S. at 490-91.



note to a foreign corporation could have a direct effect in the United States, the proposition that the court uses *Verlinden* to support.<sup>96</sup>

The *L'Europeenne* court then discussed the public policy considerations in determining that Venezuela's intervention had a direct effect in the United States.<sup>97</sup> The court noted that in *Verlinden*, the district court was concerned that finding jurisdiction solely because credits were directed through American banks would cause foreign states to divert business from the United States to banks in foreign countries.<sup>98</sup> However, the *L'Europeenne* court then cited language from *Allied Bank Int'l v. Banco Credito Agricola de Cartago*,<sup>99</sup> to show the contrary public policy considerations; namely, that withholding jurisdiction would jeopardize New York's status as a world financial center if creditors entitled to payment in United States dollars could not avail themselves of the protection of United States courts.<sup>100</sup>

The *L'Europeenne* court stated that the fact that the consortium maintained an account in the United States and agreed to be paid in dollars was enough to "sufficiently implicate" the

96. *L'Europeenne de Banque v. La Republic de Venezuela*, 700 F. Supp. 114, 121 (S.D.N.Y. 1988).

97. The court began its discussion of the case's public policy considerations with the following quote:

Effects jurisdiction derives from a state's interest in protecting those within its borders and in governing events within its borders. Thus, to determine whether a corporation has sustained a direct effect within a particular state a court must inquire whether the corporation, by its activity vis-a-vis the potential forum state, sufficiently implicates that state's interest in protecting persons within its territory.

*L'Europeenne de Banque*, 700 F. Supp. at 121 (quoting Note, *Effects Jurisdiction*, *supra* note 57, at 512).

98. *Id.* at 121-22 (citing *Verlinden v. Central Bank of Nigeria*, 488 F. Supp. 1284, 1298 (S.D.N.Y. 1980)).

99. 757 F.2d 516 (2d Cir. 1985), *cert. dismissed*, 473 U.S. 934 (1985). For a further discussion of *Allied Bank*, see *infra* notes 137-41 and accompanying text.

100. The court stated that:

The United States has an interest in maintaining New York's status as one of the foremost commercial centers in the world. Further, New York is the international clearing center for United States dollars . . . . The United States has an interest in ensuring that creditors entitled to payment in the United States in United States dollars under contracts subject to the jurisdiction of United States courts may assume that, except under the most extraordinary circumstances, their rights will be determined in accordance with recognized principles of contract law.

*L'Europeenne de Banque*, 700 F. Supp. at 122 (quoting *Allied Bank v. Banco Credito Agricola de Cartago*, 757 F.2d 516, 521-22 (2d Cir. 1985)).

interest of the United States and, therefore, Venezuela's repudiation caused a direct effect in the United States.<sup>101</sup> Having found that Venezuela had engaged in commercial activity, and that this activity had a direct effect in the United States, the court addressed the question of whether it had personal jurisdiction over Venezuela, and held that it did not.<sup>102</sup> The case was then dismissed.<sup>103</sup>

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101. *Id.*

102. *Id.* at 122-25. The court began its personal jurisdiction analysis by declining to hold Venezuela bound by SFC's agreement to consent to personal jurisdiction in the Southern District of New York. *Id.* at 123. It ruled that Venezuela had not waived its claim to sovereign immunity, either expressly or impliedly, because it had taken over SFC to avert a potentially disastrous financial crisis, and because public policy required that the waiver provision of the FSIA be construed narrowly. (citing *Frolova v. U.S.S.R.*, 761 F.2d 370, 377 (7th Cir. 1985) (*per curiam*); *Colonial Bank v. Compagnie Generale Maritime et Financiere*, 645 F. Supp. 1457, 1461 (S.D.N.Y. 1986); see also 1 J. MOORE, J. LUCAS, H. FINK, D. WECKSTEIN & J. WICKER, *MOORE'S FEDERAL PRACTICE* para. 0.66[2.-2] at 700.164 (2d ed. 1988) (in connection with determining what acts constitute implied waiver of sovereign immunity by foreign states, "it is to be noted that in litigation involving an American State's immunity under the Eleventh Amendment the courts have recognized implied waivers, but on the whole have taken a cautious approach in defining the conduct that will result in a waiver").

Having found that the waiver provision of the FSIA did not apply, the court attempted to determine whether Venezuela had sufficient contacts with the United States to demonstrate the existence of personal jurisdiction. *Id.* at 123-25. The court (citing *Asahi Metal Indus. Co. v. Superior Court*, 480 U.S. 102 (1987)), noted that "the exercise of jurisdiction must comport with traditional notions of fair play and substantial justice." *Id.* at 123.

The consortium alleged three contacts between the defendants and the United States. The court noted that the contacts that are appropriate to consider are national in scope: "the proper inquiry in determining personal jurisdiction in a case involving federal rights is one directed to the totality of a defendant's contacts throughout the United States." *Id.* at n.10 (quoting *Max Daetwylere Corp. v. R. Meyer*, 762 F.2d 290, 293 (3d Cir. 1985)). The first alleged contact was the New York properties, which the complaint alleged Perez Sandoval acquired with funds he "systematically and unlawfully converted from SFC or its subsidiaries." *Id.* at 124 (quoting complaint para. 29). The second alleged contact was Perez Sandoval's transactions with a Miami bank in connection with the purchase of shares in a Florida corporation. *Id.* (quoting complaint paras. 24-28). The third alleged contact was that the payment from SFC to the plaintiffs was to occur in New York. *Id.* (quoting complaint para. 19).

The court held that, inasmuch as there was no allegation in the complaint that any representative of Venezuela had any contact with the United States in connection with the intervention over SFC, and that none of the contacts alleged were sufficient to confer personal jurisdiction over Venezuela, *id.* at 124-25, it would not comport with "traditional notions of fair play and substantial justice" to subject Venezuela to the court's personal jurisdiction and the complaint was therefore dismissed without prejudice. *Id.* at 125.

103. *Id.*

### C. Analysis

*L'Europeenne* contributes to a pattern of inconsistency in the case law addressing the issue of what constitutes commercial activity by a foreign sovereign. Instead of applying the substantial body of case law since the enactment of the FSIA, however, the court relied on a case decided in 1927 to show that Venezuela's intervention constitutes commercial activity. It also contradicted both congressional intent and the case law in determining when a foreign sovereign's commercial activities have a direct effect in the United States. Congress intended that the direct effect clause be applied strictly, and United States courts have enforced the clause that way. The *L'Europeenne* opinion contravenes that line of cases.

#### 1. Commercial Activity

In finding that Venezuela's takeover of the operations of SFC constituted commercial activity under the FSIA, the court relied solely on *Metropolitan Savings Bank and Trust v. Farmer's State Bank*,<sup>104</sup> a case decided forty-nine years before the passage of the FSIA. In *Metropolitan Savings*, the plaintiff bank sued to recover on a certificate of deposit issued by the defendant bank, which at the time of suit was temporarily operated by the state of Nebraska.<sup>105</sup> The court denied the defendant's claim of sovereign immunity, holding that the temporary operation of the bank through a state agency, without disturbing its corporate existence or identity, would not enable the bank to assert sovereign immunity.<sup>106</sup>

A more logical standard to determine whether a state's conduct constitutes commercial activity would be the one described in *MOL*: if the activity is one that cannot be performed by a private party, the foreign sovereign's application for immunity

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104. 20 F.2d 775 (8th Cir. 1927), *cert. denied*, 276 U.S. 624 (1928).

105. *Metropolitan Savings*, 20 F.2d at 775-76.

106. *Id.* The ruling by the court in *Metropolitan Savings* is on weak ground insofar as it relied on the prior Supreme Court rulings regarding the permanent takeover of banks. Regardless of whether it is a traditional state function to run private banks, it clearly is a traditional state function to ensure the safety and soundness of banks operating within that state's jurisdiction. It does not necessarily follow that because a permanent takeover of a bank is not protected by sovereign immunity, a temporary takeover to ensure the safety of the bank's deposits is similarly unprotected.

should be granted.<sup>107</sup> In *Letelier v. Republic of Chile*,<sup>108</sup> the Second Circuit, applying this test, stated that the "[i]nquiry therefore ordinarily focuses on whether the specific acts are those that private persons normally perform, [or that] an individual would customarily carry out for profit."<sup>109</sup> The court ruled that the Chilean national airline, which was sued for transporting the assassins of the plaintiff's decedent to the United States, was entitled to immunity because, under the commercial activities exception, property could only be attached if the activity causing injury was commercial in nature and that "an act of political terrorism is not the kind of commercial activity Congress anticipated."<sup>110</sup> The court found that the presence or absence of a profit motive is a significant factor in determining whether an activity is commercial.<sup>111</sup>

Government activities should not be held to constitute commercial activity if a private party could not have carried out that activity. In *MOL v. People's Republic of Bangladesh*,<sup>112</sup> the court held that Bangladesh was entitled to sovereign immunity because the activity complained of, breach of a contract for the export of monkeys to be used for scientific research, was not

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107. *MOL v. People's Republic of Bangladesh*, 572 F. Supp. 79, 84 (1983), *aff'd*, 736 F.2d 1326 (9th Cir.), *cert. denied*, 469 U.S. 1037 (1984).

108. 748 F.2d 790 (2d Cir. 1984), *cert. denied*, 471 U.S. 1125 (1985).

109. *Letelier*, 748 F.2d at 797. At the trial level, the plaintiffs brought a wrongful death action against the Republic of Chile as survivors of the former Chilean Ambassador to the United States who was killed as a result of a car bomb in Washington, D.C. *Letelier v. Republic of Chile*, 488 F. Supp. 665 (D.D.C. 1980). The plaintiffs were awarded a default judgment (the district court found subject matter jurisdiction under the tort exception to immunity in section 1605(a)(5) of the FSIA). The plaintiffs attempted to enforce the judgment on property belonging to the Chilean national airline, arguing that the commercial activity exception applied because the airline had brought the assassins to the United States. *Letelier v. Republic of Chile*, 567 F. Supp. 1490 (S.D.N.Y. 1983). The court thereafter held that the plaintiff creditors were entitled to an appointment of a receiver of the airline's assets. *Letelier v. Republic of Chile*, 575 F. Supp. 1217 (S.D.N.Y. 1983). The Second Circuit subsequently reversed the district court's decision. *See Letelier*, 748 F.2d at 790.

110. *Id.* at 799.

111. *Id.* at 797.

112. 736 F.2d 1326 (9th Cir.), *cert. denied*, 469 U.S. 1037 (1984). In *MOL*, the Bangladesh Ministry of Agriculture granted a United States corporation a license to capture and export rhesus monkeys. The agreement specified quantities and prices, required the corporation to build a breeding farm in Bangladesh and was conditioned upon exclusive use of the monkeys for scientific research. Bangladesh reserved the right to terminate the agreement without notice if MOL failed to fulfill its obligations. After two years Bangladesh terminated the agreement because MOL allegedly failed to build the breeding farm and allegedly sold the monkeys to the United States armed services for radiation experiments. *Id.* at 1329-30.

commercial in nature.<sup>113</sup> The court ruled that the agreement being terminated was one that only a sovereign could have made because the contract concerned the right to regulate imports, exports, and natural resources, which are sovereign functions, and thus immunity was proper.<sup>114</sup>

The *L'Europeenne* court's holding that Venezuela's intervention in a domestic bank's affairs constitutes commercial activity contradicts this test and results in the realization of a Congressional concern when the FSIA was passed, that United States courts would be converted to international courts of claims as a result of the Act's passage.<sup>115</sup> The test used in *MOL* includes the idea that, if in performing the act the sovereign had no profit motive, as the *L'Europeenne* court concedes Venezuela did not,<sup>116</sup> the activity is not commercial within the meaning of the FSIA.<sup>117</sup>

## 2. Direct Effect

Having found that Venezuela had engaged in commercial activity, the *L'Europeenne* court relied in part on *Texas Trading* to support its conclusion that this activity had a direct effect in the United States.<sup>118</sup> An important difference between *Texas Trading* and *L'Europeenne*, however, is that Texas Trading was a United States company, not a foreign company, as the plaintiff banks in the consortium were. The fact that Texas Trading was a United States corporation was critical to the court's ruling that Nigeria's repudiation caused a direct effect in the United States: the court noted that the question of "whether a failure to pay a foreign corporation in the United States or a United States corporation abroad creates an effect in the United States under [the commercial activities exception]" was not before it.<sup>119</sup>

The *L'Europeenne* court also relied on *Verlinden B.V. v.*

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113. *MOL*, 736 F.2d at 1329.

114. *Id.*

115. See *supra* note 26 and accompanying text.

116. *L'Europeenne de Banque v. La Republic de Venezuela*, 700 F. Supp. 114, 119 (S.D.N.Y. 1988).

117. *Letelier v. Republic of Chile*, 748 F.2d 790, 797 (2d Cir. 1984), *cert. denied*, 471 U.S. 1125 (1985); *United States v. County of Arlington, Va.*, 702 F.2d 485, 488 (4th Cir. 1983).

118. *L'Europeenne de Banque*, 700 F. Supp. at 121.

119. *Texas Trading & Milling v. Federal Republic of Nigeria*, 647 F.2d 300, 312 (2d Cir. 1981), *cert. denied*, 454 U.S. 1148 (1982).

*Central Bank of Nigeria*<sup>120</sup> in support of its conclusion that there was a direct effect in the United States, stating that *Verlinden* allows for the possibility that injury to a foreign plaintiff can have a direct effect in the United States.<sup>121</sup> The question in *Verlinden*, however, was only whether a foreign citizen or corporation could ever sue a foreign defendant in United States courts under the FSIA.<sup>122</sup> The Supreme Court, while holding that they could, specifically left open the question of whether the facts in that particular case allowed for subject matter jurisdiction under the Act.<sup>123</sup>

*Verlinden* arose out of the same set of transactions as *Texas Trading*.<sup>124</sup> The plaintiff was a Dutch corporation suing the Republic of Nigeria for the anticipatory breach of a letter of credit for the purchase of a shipment of cement.<sup>125</sup> *Verlinden* alleged jurisdiction under the FSIA.<sup>126</sup> Both the district court and the Second Circuit held that Nigeria was entitled to immunity under the FSIA.<sup>127</sup> The Supreme Court unanimously reversed, holding that on the Act's face, foreign plaintiff's are allowed to sue foreign sovereigns in federal court, provided the substantive standards of the Act are satisfied.<sup>128</sup> The *Verlinden* court expressed no opinion as to whether financial injury to a foreign plaintiff could ever have a direct effect in the United States. The court then remanded the case to the Second Circuit to determine

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120. 461 U.S. 480 (1983).

121. *L'Europeenne de Banque*, 700 F. Supp. at 121.

122. *Verlinden*, 461 U.S. at 489.

123. *Id.* at 497-98.

124. See *supra* notes 30-38 and accompanying text.

125. *Verlinden v. Central Bank of Nigeria*, 461 U.S. 480, 482 (1983).

126. The district court, while holding that the Act permitted actions by foreign plaintiffs where both defendant and plaintiff were aliens, dismissed the action on the ground that none of the exceptions to sovereign immunity specified in the Act applied. *Verlinden v. Central Bank of Nigeria*, 488 F. Supp. 1284 (S.D.N.Y. 1981). In ruling specifically that Nigeria's repudiation of the contract did not have a direct effect in the United States, the court, after quoting the test given in *Harris v. VAO Intourist Moscow*, 481 F. Supp. 1056, 1062-63 (E.D.N.Y. 1979), held that the locus of the injury is dispositive of jurisdiction. *Verlinden*, 488 F. Supp. at 1298. Under this test, the court held that the effect on *Verlinden* in the United States was insufficient to permit the exercise of jurisdiction over Nigeria. *Id.*

The Second Circuit affirmed, but on the ground that the constitutional power of the federal courts to exercise jurisdiction over suits either arising under federal law or the Diversity Clause does not extend to suits brought by foreign plaintiffs against a foreign sovereign. *Verlinden v. Central Bank of Nigeria*, 647 F.2d 320 (2d Cir. 1981).

127. *Verlinden*, 488 F. Supp. at 1284; *Verlinden*, 647 F.2d at 320.

128. *Verlinden*, 461 U.S. at 489.

whether jurisdiction existed under the Act itself.<sup>129</sup> The Supreme Court's opinion did not address the jurisdictional requirement that the act by a foreign sovereign have a direct effect in the United States.<sup>130</sup> Thus, the *L'Europeenne* court relied on an opinion that it conceded "did not decide this particular question."<sup>131</sup> Although *Verlinden* does allow for a finding of direct effect, it also holds that the substantive standards of the Act must be met.<sup>132</sup> The substantive standard required to meet the direct effect test is the one provided by Section 18.<sup>133</sup> In *L'Europeenne*, those standards, as applied by United States courts since the Act was passed, were not met.

The line of cases since the passage of the FSIA leads to the conclusion that Venezuela's intervention into SFC's operations did not have a direct effect in the United States because it was not sufficiently substantial or foreseeable as required by Section 18. Although the Second Circuit has never formally adopted this standard, the Court of Appeals for the Fifth, Sixth, Seventh, Ninth, and District of Columbia Circuits have all held that Section 18 is the standard Congress intended.<sup>134</sup>

After citing *Verlinden* to support the proposition that financial injury to a foreign corporation could have a direct effect in the United States, the court quoted the Second Circuit's opinion in *Allied Bank Int'l v. Banco Credito Agricola de Cartago*<sup>135</sup> to show the public policy concerns that New York's position as a financial center would be harmed if creditors in LEB's position could not bring suit in the United States.<sup>136</sup> *Allied Bank* con-

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129. *Id.* at 497-98.

130. *Id.* at 490.

131. *L'Europeenne de Banque v. La Republic de Venezuela*, 700 F. Supp. 114, 121 (S.D.N.Y. 1988).

132. *Verlinden v. Central Bank of Nigeria*, 461 U.S. 480, 490-91 (1983).

133. *See supra* note 13.

134. *See Zernicek v. Brown & Root, Inc.* 826 F.2d 415, 417-18 (5th Cir. 1987) (effects of foreign state's conduct must be "substantial" and a "direct and foreseeable" result of that conduct to support jurisdiction under the FSIA); *Gould v. Pechiney Ugine Kuhlmann*, 853 F.2d 445, 453 (6th Cir. 1988). *See infra* notes 70-76. *See also* *Rush-Presbyterian-St. Luke's Medical Center v. Hellenic Republic*, 877 F.2d 574, 581 (7th Cir.), *cert. denied*, 110 S.Ct. 333 (1989); *America West Airlines, Inc. v. GPA Group, Ltd.*, 877 F.2d 793, 798-99 (9th Cir. 1989) (holding that a "foreign sovereign's activities must cause an effect in the United States that is substantial and foreseeable in order to abrogate sovereign immunity"); *Zedan v. Kingdom of Saudi Arabia*, 849 F.2d 1511, 1514 (D.C. Cir. 1988).

135. 757 F.2d 516 (2d Cir. 1984), *cert. dismissed*, 473 U.S. 934 (1985).

136. *L'Europeenne de Banque v. La Republic de Venezuela*, 700 F. Supp. 114, 122 (S.D.N.Y. 1988). For a full account of the Second Circuit's concern, see *supra* note 100.

cerned the default on an international loan from Allied to three Costa Rican banks including Banco Credito. The debtor banks defaulted on their obligations as a result of an order restricting external debt repayments which the Costa Rican Government issued during an economic crisis.<sup>137</sup> Pursuant to its loan agreement with the debtor banks, Allied sought to accelerate the outstanding payments on the loans in the face of the debtor's default.<sup>138</sup> The district court refused to grant summary judgment to Allied on the grounds that the Costa Rican banks had a strong Act of State doctrine defense.<sup>139</sup> The Second Circuit reversed, however, and granted Allied summary judgment, citing in part the public policy concern the *L'Europeenne* court mentioned: the United States has an interest in protecting creditors who make loans in dollars.<sup>140</sup> Ironically, commentators have criticized *Allied* as threatening to New York's position as a financial center because it could have the effect of diverting business away from New York banks.<sup>141</sup>

To assert jurisdiction under the direct effect clause, courts must hold that the direct effect exists either where the corporate entity is located, where the corporation is incorporated or where it does business,<sup>142</sup> or the location of the act or omission that causes the injury, either the designated place of defendant's performance, or the place where the defendant's breach occurred.<sup>143</sup> In *LEB*, the first alternative would lead to a country where one of the banks in the consortium was incorporated or did business, and the second alternative would lead to Venezuela, where the government's intervention in the management of SFC and its repudiation of the loan occurred. Neither alternative would allow the suit to be heard in the United States.

Where the plaintiffs have been corporations, courts have applied the test imposed by Section 18 strictly.<sup>144</sup> In *MINE* for ex-

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137. *Allied Bank Int'l v. Banco Credito Agricola de Cartago*, 566 F. Supp. 1440, 1442 (S.D.N.Y. 1983).

138. *Allied Bank*, 566 F. Supp. at 1442.

139. *Id.* at 1443-44.

140. *Allied Bank Int'l v. Banco Credito Agricola de Cartago*, 757 F.2d 516, 521-22 (2d Cir. 1984). See *supra* note 100.

141. Note, *Debt Restructuring Process*, 17 N.Y.U. J. INT'L L. & POL. 613, 626 (1985).

142. Note, *Effects Jurisdiction*, *supra* note 57, at 510.

143. Note, *Effects Jurisdiction*, *supra* note 57, at 510.

144. It has been argued that when the plaintiff is a citizen, even a United States citizen, courts have applied the test too strictly. See, e.g., Comment, *Martin v. South Africa*, *supra* note 10, at 153-54. Comment, *Martin v. South Africa* argues that a congressional amendment is needed to protect United States citizens injured abroad by acts



ample, the court held that profits lost by Global, a third party United States company, did not pass the test set forth by Section 18.<sup>145</sup> It was concluded that Global's loss was not a sufficiently direct result of the defendant state's breach because Global's "profit anticipating involvement" was not contemplated by the contract between the foreign plaintiff and foreign state defendant.<sup>146</sup> In *Gould*, the plaintiff could point to specific harm that occurred as a result of the act of the foreign sovereign as being sufficiently substantial, direct or foreseeable: the plaintiff allegedly lost profits as a result of France's actions.<sup>147</sup> No such effect in the United States took place as a result of Venezuela's actions. In *L'Europeenne*, the only connection with the United States were the loan to SFC that was to be repaid in dollars and the presence of the bank account in New York that was to be used to repay the loan.<sup>148</sup> Neither of these factors sufficiently implicates United States interests in protecting persons or corporations within its territory.

In determining whether financial injury to a corporation is sufficiently direct to meet the test imposed by the FSIA, a court should determine whether the corporation has sufficiently manifested itself within the United States so that the loss sustained by the corporation may be deemed to have been sustained by a United States corporation. Activities that would subject a foreign corporation to suit as a defendant are not necessarily sufficient to allow courts to consider that corporation to be located within the United States. Thus, the fact that the corporation contracted to provide goods to someone located within the United States or sent agents into the United States, is by itself insufficient to attribute the location of the corporation's injury to that state.<sup>149</sup> In contrast, the presence of an office or a factory within the United States would probably be sufficient.<sup>150</sup> In de-

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of foreign sovereigns and left without recourse because of courts application of direct effect exception. *Id.* at 171-73.

145. *Maritime Int'l Nominees Establishment (MINE) v. Republic of Guinea*, 693 F.2d 1094, 1111 (D.D.C. 1982). For a discussion of the facts and holding of the case, see *supra* notes 63-69 and accompanying text.

146. *MINE*, 693 F.2d at 1111.

147. *Gould, Inc. v. Pechiney Ugine Kuhlmann*, 853 F.2d 445 (6th Cir. 1988). For a discussion of the facts and holding of the case, see *supra* notes 70-76 and accompanying text.

148. *L'Europeenne de Banque v. La Republic de Venezuela*, 700 F. Supp. 114, 125 (S.D.N.Y. 1988).

149. Note, *Effects Jurisdiction*, *supra* note 57, at 513.

150. Note, *Effects Jurisdiction*, *supra* note 57, at 513.

termining whether the injury has had a direct effect in the United States, a court should determine whether it is reasonable to ascribe the loss sustained by the corporation to its presence within the United States.

Although the court found that Venezuela did not have sufficient contacts with the United States to allow the court to exercise personal jurisdiction over it, its expansion of the definitions of commercial activity and of direct effect poses several problems. While it is true that the United States will sometimes have an interest in applying United States laws in lawsuits between foreign parties when claiming jurisdiction over foreign sovereigns, care should be taken not to unnecessarily harm United States foreign policy or financial interests.<sup>151</sup>

### 3. Harm to the United States as Financial Center

Perhaps the most important ramification of the court's opinion is that parties entering into international contracts will divert business from banks in the United States to banks in foreign countries in order to avoid being subject to the jurisdiction of United States courts. As the international financial system moves toward a system where London and Tokyo become equally as accessible as New York, parties will be inclined to transfer their business from one financial center to another to avoid hostile legal environments. As the district court in *Verlinden* stated: "[S]olicitude for New York's 'preeminent financial position' should induce the courts to forbear the exercise of jurisdiction in close cases."<sup>152</sup> New York's position would be significantly weakened if the mere designation of American banks for payment subjects foreign sovereigns to the jurisdiction of United States courts.<sup>153</sup> It is true that very few elements of a jurisdiction's business environment will, by themselves, have a decisive effect in determining where financial transactions are conducted. Nevertheless, particular laws or decisions may have exactly this type of determinative impact.<sup>154</sup>

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151. Note, *Foreigner — Foreign State suits*, *supra* note 1, at 1870. For example, some United States laws "are designed to deter undesirable behavior affecting the United States." *Id.*

152. *Verlinden v. Central Bank of Nigeria*, 488 F. Supp. at 1298 (quoting J. Zeevi & Sons v. Grindlays Bank (Uganda), 37 N.Y.2d 220, 227, *cert. denied*, 423 U.S. 866 (1975)).

153. *Id.*

154. See Gordon, *The Mandatory Structure of Corporate Law*, 89 COLUM. L. REV. 1549, 1552-53 (1989).

Businesses require a predictable legal environment, especially when their actions may subject them to suit in the United States. It should be possible to know what constitutes commercial activity and when that activity has a direct effect. As originally adopted and interpreted, the FSIA attracted international financial transactions to New York and, in response to its passage, the British State Immunity Act of 1978 was passed, partly out of fear that the FSIA made New York a more attractive location than London for the transaction of business involving foreign states.<sup>155</sup> Decisions such as *L'Europeenne* dilute these benefits.

#### 4. Foreign Policy Considerations

Other objections to the broad definition of commercial activity and direct effect are that it may precipitate retaliatory liability abroad,<sup>156</sup> and that it could open United States courts to a flood of international litigation in which no United States interests are implicated.<sup>157</sup> Even if relatively few suits are brought by foreign plaintiffs against foreign sovereigns in United States courts these suits will nevertheless be important because they often involve significant amounts of money.<sup>158</sup>

Additionally, since states have a particular interest in having local controversies decided in its own courts,<sup>159</sup> a suit brought in a United States court might be brought more appropriately in another forum since that forum has a greater interest in the suit. If, as in *L'Europeenne*, no significant United States interest is implicated, the burden on United States courts of trying such a suit may make more appropriate dismissal of the suit in favor of the alternative jurisdiction.<sup>160</sup>

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155. Comment, *The State Immunity Act 1978*, 42 MOD. L. REV. 72, 72-73 (1979).

156. See Born, *Reflections on Judicial Jurisdiction in International Cases*, 17 GA. J. INT'L L. 1, 33 (1987).

157. See, e.g., *Vencedora Oceanica Navigacion v. Compagnie Nationale Algerienne de Navigation*, 730 F.2d 195 (5th Cir. 1984) (suit by foreign plaintiff against the Republic of Algeria dismissed because no nexus existed between the plaintiff's claim and commercial activity carried on in the United States by the Foreign defendant).

158. Note, *Foreigner — Foreign State Suits*, *supra* note 1, at 1861 n.6 (citing *Verlinden v. Central Bank of Nigeria*, 488 F. Supp. 1284, 1288 (claim for more than \$4.5 million); *Ipitrade Int'l, S.A. v. Federal Republic of Nigeria*, 465 F. Supp. 824, 825 (D.D.C. 1978) (award of approximately \$9 million)).

159. Note, *Foreigner — Foreign State Suits*, *supra* note 1, at 1872.

160. Note, *Foreigner — Foreign State Suits*, *supra* note 1, at 1872. See also Comment, *Forum Non Conveniens, Injunctions Against Suit and Full Faith and Credit*, 29 U. CHI. L. REV. 740, 749 (1962) (crowding of local dockets weighs in favor of forum non

Also, for a United States court to exercise jurisdiction in a foreigner-foreign state suit may adversely affect United States foreign policy interests by having a branch of the United States Government pass judgment on the actions of a foreign sovereign. This will be especially true when the laws of sovereign immunity in other nations differ from the rule established by the FSIA. Foreign states are likely to object to the exercise of jurisdiction over them in United States courts that would not be allowed in their own courts.<sup>161</sup> The United States already is commonly accused of infringing on the sovereignty of other nations by applying American law extraterritorially.<sup>162</sup> This charge is likely to be raised with special force when United States law is enforced against a foreign state. Finally, even states with no objection in principle to the extraterritorial application of United States law may disagree with the application of those rules in particular cases.<sup>163</sup>

#### IV. CONCLUSION

Congress enacted the FSIA to regularize the process of obtaining jurisdiction over foreign sovereigns in United States courts. If parties can correctly anticipate when they will be subject to the laws of the United States, the Act will have served its purpose; it will promote judicial economy and efficiency, and will promote the use of the United States as an international commercial center. However, decisions that expand existing case law on such amorphous bases as "public policy," rather than the language of the Act and established precedent, have the potential to do serious harm to the role of the United States as a center of international finance and to United States foreign policy interests.

The *L'Europeenne* decision, if it is followed in future cases, has the potential to do exactly this kind of harm. Foreign sovereigns will seek to make payments in Pounds, Yen, or Deutch Marks rather than dollars, in banks in London, Tokyo, or

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convenient dismissal in primarily foreign controversies).

161. Note, *Foreigner — Foreign State Suits*, *supra* note 1, at 1874; Editorial Comment, *Sovereign Immunity — The case of the "Imias,"* 68 AM. J. INT'L L. 280, 283 (1974) (describing Cuba's assertion to the State Department that Cuba was entitled to immunity under international law with respect to its commercial acts, despite "unilateral attempt of the United States to modify that doctrine").

162. Note, *Foreigner — Foreign State Suits*, *supra* note 1, at 1874.

163. Note, *Foreigner — Foreign State Suits*, *supra* note 1, at 1874.

Frankfurt rather than in New York. By temporarily intervening in the affairs of the largest bank in Venezuela, Venezuela was engaging in one of the most basic and traditional of sovereign functions: regulating its domestic commerce and ensuring the safety of its banking system. Even in the event that Venezuela's actions were actually commercial, to hold that by denying payment to a foreign creditor with no connections to the United States Venezuela has caused a direct effect in the United States stretches the definition of that term well beyond the established case law and what Congress intended.

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