

# ARTICLES

## SELECTED ISSUES IN SOVEREIGN DEBT LITIGATION

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What happens when a sovereign debtor<sup>1</sup> fails to make principal or interest payments due under a restructuring, rescheduling, new money or other financing agreement, or declares a moratorium on repayment of foreign debt, and one or more of its foreign creditors decides to pursue its various legal remedies to compel repayment of that debt? In this Article we discuss in what court such an action is likely to be litigated and how such an action might differ from an action brought against a private debtor. We also examine what body of law a court is likely to apply and certain defenses that a sovereign debtor may have available to such an action because of its sovereign status, that a private debtor could not employ.<sup>2</sup>

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<sup>1</sup> A sovereign debtor is a state, or a political subdivision, agency or instrumentality of a state, which has borrowed money pursuant to a loan or other financing agreement.

<sup>2</sup> Although not addressed here, it has been suggested that Article VIII, section 2(b) of the Bretton Woods Agreement, Dec. 27, 1945, 60 Stat. 1401, 1411, T.I.A.S. No. 1501, at 12, 2 U.N.T.S. 39, 66, 68, may, in proper circumstances, provide a defense to an action brought in the United States against a sovereign debtor under a loan agreement.

Article VIII, section 2(b) provides that "[e]xchange contracts which involve the currency of any member and which are contrary to the exchange control regulations of that member maintained or imposed consistently with this Agreement shall be unenforceable in the territories of any member." *Id.*

To date, United States courts have not enforced section 2(b) as a defense to an action on a sovereign debt agreement. Instead, United States courts have narrowly construed the term "exchange contract" to mean only those transactions which are "contracts for the exchange of one currency against another or one means of payment against another," explicitly excluding international loan agreements. *Libra Bank Ltd.*

## 1. INTRODUCTION: NEW YORK COURT PROCEDURES

A sovereign debtor's substantive liability under its financing agreements and the amenability of its assets to attachment, execution or set-off could be decided in the context of judicial proceedings, which could be commenced in any court where the sovereign debtor is subject to jurisdiction.<sup>3</sup> Litigation resulting from a default under a financing agreement is frequently brought in state and federal courts sitting in New York, since most money center banks and their counsel are located there and since financing agreements typically provide that New York law governs the agreement and that the sovereign debtor submits to the jurisdiction of state and federal courts in New York. Therefore, it is useful to summarize the general course that such proceedings would likely take in New York.

If an action is commenced in any United States court against a borrower that is a "foreign state" (within the meaning of the Foreign Sovereign Immunities Act of 1976 ("FSIA")),<sup>4</sup> either directly under any financing agreement or to enforce a foreign judgment thereunder, the defendant/sovereign debtor would have sixty days to file a responsive pleading or motion.<sup>5</sup> A plaintiff (particularly if it had already ob-

v. Banco Nacional de Costa Rica, 570 F. Supp. 870, 897 (S.D.N.Y. 1983) (quoting J. Gold, *THE FUND AGREEMENT IN THE COURTS: VOLUME II* 425 (1982)). See also *J. Zeevi & Sons, Ltd. v. Grindlays Bank (Uganda) Ltd.*, 37 N.Y.2d 220, 333 N.E.2d 168, 371 N.Y.S.2d 892 (1975), cert. denied, 423 U.S. 866 (1975); *Banco do Brasil v. A.C. Israel Commodity Co.*, 12 N.Y.2d 371, 239 N.Y.S.2d 872 (1963), cert. denied, 376 U.S. 906 (1964). By contrast, some European courts have construed the term "exchange contract" contained in section 2(b) broadly to include all contracts that "in any way affect a country's exchange resources," thereby potentially including international loan agreements in the definition of exchange contracts. Schwab, *The Unenforceability of International Contracts Violating Foreign Exchange Regulations: Article VIII, Section 2(b) of the International Monetary Fund Agreement*, 25 VA. J. INT'L L. 967, 977 (1985) (citations omitted). See generally Nurick, *The International Monetary Fund Articles of Agreement*, in *JUDICIAL ENFORCEMENT OF INTERNATIONAL DEBT OBLIGATIONS* 107 (D. Sasson & D. Bradlow eds. 1987); Zamora, *Recognition of Foreign Exchange Controls in International Creditors' Rights Cases: The State of the Art*, 21 INT'L LAW. 1055 (1987).

For a discussion of the doctrines of act of state and comity, which could in proper circumstances provide a defense to liability of a sovereign debtor, see Buchheit, *Act of State and Comity: Recent Developments*, in *JUDICIAL ENFORCEMENT OF INTERNATIONAL DEBT OBLIGATIONS* 95 (D. Sasson & D. Bradlow eds. 1987).

<sup>3</sup> See *infra* notes 12-29 and accompanying text.

<sup>4</sup> 28 U.S.C. §§ 1602-1611 (1988). Under the FSIA, a foreign state "includes a political subdivision of a foreign state or an agency or instrumentality of a foreign state" which is at least majority-owned by a foreign state or political subdivision thereof. 28 U.S.C. § 1603 (1988).

<sup>5</sup> 28 U.S.C. § 1608(d) (1988). Such an action could be brought initially in either state or federal court. However, if it were commenced in state court, the foreign sovereign defendant would in all probability want to remove the case to federal court, and could do so automatically by filing a removal petition within thirty days of receiving the

tained a foreign judgment) would probably make a motion for summary judgment shortly after initiating suit, alleging that no material questions of fact exist and seeking a determination of liability based solely upon the documentary record. The defendant would then have to respond to this motion in ten days, but probably not earlier than the sixtieth day after commencement of the action.<sup>6</sup>

A motion for summary judgment would be submitted to the judge for a decision on the merits.<sup>7</sup> A court will ordinarily enforce a foreign judgment previously rendered under an agreement, unless the defendant could demonstrate that the foreign court lacked jurisdiction, the foreign court failed to afford it proper notice of the proceedings, or that the judgment was fraudulently obtained, all of which are unlikely.<sup>8</sup>

If a court in the United States enters a final judgment adverse to a sovereign defendant, the plaintiff cannot seek to execute on the judgment until the court has "determined that a reasonable period of time has elapsed following the entry of judgment. . . ."<sup>9</sup> The purpose of this provision is to give a foreign state defendant an opportunity to avoid the embarrassment of execution by voluntarily paying the judgment.

The defendant has thirty days to appeal from any judgment. However, during the pendency of any appeal, once the "reasonable time" for voluntary payment of the judgment has elapsed, unless a court-ordered stay of judgment is obtained, assets of the defendant are subject to execution.<sup>10</sup> Typically, such a stay cannot be obtained without posting a bond. It would be difficult, if not impossible, for a foreign sovereign defendant which had defaulted under its financing agreements to post an adequate bond, unless it were to provide cash in the full amount of the judgment to the bonding company as collateral. This course of action might be unwise, however, because it would make as-

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initial service of process in the suit. 28 U.S.C. §§ 1441(d), 1446(b) (1988). See *infra* notes 54-58 and accompanying text for a discussion of whether this right of removal can be waived by a foreign state. The balance of the discussion in this section assumes that proceedings will be conducted in federal court, although the rules governing suit, attachment, and execution under the FSIA apply to actions in both state and federal courts.

<sup>6</sup> A plaintiff is entitled to move for summary judgment twenty days after commencement of suit. FED. R. Civ. P. 56(a). However, the time for a sovereign defendant to respond to such a motion would probably be extended until the expiration of the sixty day period for filing a responsive pleading or motion under the FSIA.

<sup>7</sup> For a discussion of the law the court is likely to apply, see *infra* notes 107-36 and accompanying text.

<sup>8</sup> See N.Y. Civ. PRAC. L. & R. 5301-5309 (McKinney 1978 & Supp. 1989).

<sup>9</sup> 28 U.S.C. § 1610(c) (1988).

<sup>10</sup> For a discussion of when assets of an agency or instrumentality of a foreign state are deemed to be attachable as assets of that foreign state, see *infra* notes 179-88 and accompanying text.

sets available for execution in the event of an unsuccessful appeal.

Discovery of the defendant would probably be permitted to enable the plaintiff to locate assets for execution in the United States and elsewhere. The interest of the defendant in not disclosing this information might lead to its refusal to comply with such discovery requests, which would in turn be likely to lead to various court-imposed sanctions. The efficacy of such sanctions would ultimately depend upon the presence of property in the United States belonging to the defendant that is susceptible to attachment or execution under the FSIA.

## 2. CHOICE OF FORUM AND GOVERNING LAW CLAUSES: DO THEY WORK?

Parties to sovereign debt agreements have a particular interest in the ability to select in advance both the law that governs the parties' relationship and the forum or fora in which any disputes arising under the agreement will be resolved. The desirability of making a binding choice of governing law is clear: the meaning of even a seemingly unambiguous agreement depends ultimately on the significance that the governing law gives to the parties' words. Unless the parties can agree on that law in advance of any dispute, the very meaning of the agreement and the parties' rights and obligations thereunder will be uncertain.

For similar reasons, it is to the parties' advantage to ensure that one or more acceptable jurisdictions will be available to resolve any claim arising under a sovereign debt agreement. Some potential fora may be unfamiliar with the law the parties have chosen to govern the transaction, making their interpretation and application of that law unpredictable. Some courts may be required by their own law to decide the case under a different law than that selected by the parties, and thus may apply an unforeseen body of law to the dispute. Moreover, advance selection of an exclusive forum for litigation reduces the risk that, in the event of litigation, a party will be forced to litigate an action in an inconvenient or unfair forum. As a result, it has become routine practice for parties to insert choice of forum and governing law clauses into sovereign debt agreements. Because New York has a well-developed body of commercial law and its courts are considered both impartial and experienced in resolving disputes arising from sophisticated commercial transactions, and because many of the lenders to foreign sovereign debtors are based in New York, such clauses often specify that the agreement shall be governed by New York law, and that any disputes arising thereunder shall be resolved in New York state or federal courts.

When a dispute arises under an agreement containing such clauses, the court before which the action has been brought must first determine the enforceability of the clauses under its own legal doctrine of conflicts of law. Conflicts law is somewhat arcane at best, but in most cases the doctrinal sound and fury signifies nothing: both New York state and federal courts look with favor upon choice of forum and governing law clauses, and generally will give effect to them. This section provides an introduction to the treatment of such clauses in the courts of New York, and highlights some areas of uncertainty in the law.

### 2.1. *Choice of Forum Clauses*

It is not surprising that, despite the advantages inherent in making a binding choice of forum in advance, once litigation is contemplated or commenced a party will frequently seek to evade the contractually selected forum in favor of one which may offer a more convenient location or a more favorable court or body of law. Hence, the question of the effect a contractual forum selection clause has may arise in an action pending in the contractual forum if the plaintiff has brought the action there and the defendant seeks to alter the forum. Another situation where the enforceability of this clause is at issue occurs when the plaintiff has begun an action in violation of an exclusive forum selection clause and the defendant seeks its dismissal or transfer to the contractual forum.<sup>11</sup> Moreover, even where neither party objects to the jurisdiction of the contractual forum, in some circumstances that forum may be unable to entertain the action.

#### 2.1.1. *The First Hurdle: Does the Court Have Jurisdiction?*

In order to entertain an action, a court must have jurisdiction over the parties to the action (personal jurisdiction),<sup>12</sup> proper venue,<sup>13</sup> and

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<sup>11</sup> A forum selection clause may be either "exclusive" or "non-exclusive." An exclusive forum selection clause stipulates an exclusive forum for all litigation arising under an agreement. Under such a clause, the parties submit to the jurisdiction of the agreed forum, and agree not to commence a legal action relating to the agreement elsewhere. In contrast, pursuant to a non-exclusive forum selection clause, the parties submit to the jurisdiction of the contractual forum, but remain free to bring an action in any other forum which has jurisdiction over the dispute. See Gruson, *Controlling Site of Litigation*, in *SOVEREIGN LENDING: MANAGING LEGAL RISK* 29-30 (M. Gruson & R. Reisner eds. 1984) (hereinafter Gruson, *Controlling Site of Litigation*).

<sup>12</sup> The FSIA, read alone, appears automatically to confer on federal courts personal jurisdiction over a "foreign state" defendant whenever subject matter jurisdiction exists under 28 U.S.C. section 1330(a) and service of process has been properly made under 28 U.S.C. section 1608. 28 U.S.C. § 1330(b) (1988). Under the statute, therefore, "subject matter jurisdiction plus service of process equals personal jurisdiction."

Texas Trading & Milling Corp. v. Federal Republic of Nigeria, 647 F.2d 300, 308 (2d Cir. 1981), *cert. denied*, 454 U.S. 1148 (1982). Under section 1330(a), subject matter jurisdiction exists with respect to every action against a foreign state to which the foreign state is not entitled to immunity. 28 U.S.C. § 1330(a) (1982).

The power of Congress to grant personal jurisdiction is, however, subject to constitutional due process limitations. "Accordingly, each finding of personal jurisdiction under the FSIA requires, in addition, a due process scrutiny of the court's power to exercise its authority over a particular defendant." *Texas Trading & Milling Corp.*, 647 F.2d at 308. A finding of personal jurisdiction is considered to comport with due process where a defendant's contacts with the forum are sufficiently extensive that the assertion of personal jurisdiction is consistent with "traditional notions of fair play and substantial justice." *International Shoe Co. v. Washington*, 326 U.S. 310, 316 (1945) (quoting *Milliken v. Meyer*, 311 U.S. 457, 463 (1940)). For purposes of the FSIA, a defendant's contacts with the United States as a whole, and not with any particular forum, are judged against the due process standard of the Fifth Amendment of the Constitution. *L'Europeene de Banque v. La Republica de Venezuela*, 700 F. Supp. 114, 123 n.10 (S.D.N.Y. 1988). *But cf. Pioneer Properties, Inc. v. Martin*, 557 F. Supp. 1354, 1358-61 (D. Kan 1983), *appeal dismissed*, 776 F.2d 888 (10th Cir. 1985) (in this federal question case, the court considered only contacts with the forum in its due process analysis). Where a defendant has consented to personal jurisdiction, due process concerns will not normally be implicated. However, where a defendant is found not to have consented freely to personal jurisdiction, a court may find that it has no personal jurisdiction over a defendant, even where the subject matter jurisdiction and service of process standards of the FSIA are satisfied. For example, in *L'Europeene de Banque*, the court held that it lacked personal jurisdiction over Venezuela because of the insufficiency of Venezuela's contacts with the United States with respect to Venezuela's assumption of management power over a failing financial institution. 700 F. Supp. at 125. The suit was based in part upon agreements (executed by the financial institution) that contained submissions to jurisdiction in New York. The court noted, "[f]orum-selection clauses are favored when they are part of a 'freely negotiated private international agreement, unaffected by fraud, undue influence, or overweening bargaining power.' Here, Venezuela did not engage in free negotiations with SFC's management regarding what obligations it was assuming when it intervened SFC." *Id.* at 123 (citation omitted).

<sup>18</sup> See 28 U.S.C. § 1391 (1988). This section provides for venue in federal court actions generally. With respect to actions against foreign states it provides:

(f) A civil action against a foreign state as defined in section 1603(a) of this title may be brought—

(1) in any judicial district in which a substantial part of the events or omissions giving rise to the claim occurred, or a substantial part of property that is the subject of the action is situated;

(2) in any judicial district in which the vessel or cargo of a foreign state is situated, if the claim is asserted under section 1605(b) of this title;

(3) in any judicial district in which the agency or instrumentality is licensed to do business or is doing business, if the action is brought against an agency or instrumentality of a foreign state as defined in section 1603(b) of this title; or

(4) in the United States District Court for the District of Columbia if the action is brought against a foreign state or political subdivision thereof.

See also N.Y. CIV. PRAC. L. & R. 503(a) (McKinney 1976) (providing for venue in New York state courts "in the county in which one of the parties resided when it was commenced; or, if none of the parties then resided in the state, in any county designated by the plaintiff.").

jurisdiction over the controversy itself (subject matter jurisdiction).<sup>14</sup> When an action is brought in the contractual forum, a well-drafted forum selection clause operates as a submission to that forum's personal jurisdiction,<sup>15</sup> and as a consent to venue in the chosen forum.<sup>16</sup> Such a consent is valid in both New York state and federal courts. In both court systems, it is well settled that parties may by agreement confer personal jurisdiction and venue on the selected court,<sup>17</sup> even though in the absence of such an agreement one or both parties would not be amenable to suit there.

The requirement that the court have subject matter jurisdiction may, in some instances, prove more troublesome. The consent of the parties cannot enlarge the subject matter jurisdiction of a court. Such jurisdiction may only be conferred by the Constitution and the statutes promulgated thereunder.<sup>18</sup> Although the United States federal district

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<sup>14</sup> Under the FSIA, subject matter jurisdiction exists with respect to every action against a foreign state to which the foreign state is not entitled to immunity. 28 U.S.C. § 1330(a) (1988).

<sup>15</sup> See *Heller Fin., Inc. v. Midwehy Powder Co.*, 883 F.2d 1286 (7th Cir. 1989). For example, such a clause might provide:

The borrower irrevocably consents that any legal action or proceeding against it or any of its property arising under or relating to this agreement may be brought in any court of the State of New York or any federal court of the United States of America located in the State of New York, and hereby submits to and accepts with regard to any such action or proceeding, for itself and in respect of its property generally and unconditionally the jurisdiction of the aforesaid courts. The Borrower irrevocably waives (i) any objection which it may now or hereafter have to the laying of the venue of any suit, action, or proceeding arising out of or relating to this agreement in the State of New York, and (ii) any claim that the State of New York is not a convenient forum for any such suit, action, or proceeding.

The clause at issue in *Credit Francais Int'l, S.A. v. Sociedad Financiera de Comercio, C.A.*, 128 Misc. 2d 564, 490 N.Y.S.2d 670 (Sup. Ct. 1985), contained essentially this language.

<sup>16</sup> Courts will construe a consent to personal jurisdiction in a forum as a consent to venue in that forum. See *Coface v. Optique du Monde, Ltd.*, 521 F. Supp. 500, 506 (S.D.N.Y. 1980). By the same reasoning, a consent to venue will sometimes be construed as a consent to personal jurisdiction in the forum. See *Richardson Greenshields Sec., Inc. v. Metz*, 566 F. Supp. 131, 133 (S.D.N.Y. 1983).

<sup>17</sup> *National Equip. Rental, Ltd. v. Szukhent*, 375 U.S. 311, 315-16 (1964); *Neirbo Co. v. Bethlehem Shipbuilding Corp.*, 308 U.S. 165, 167-68 (1939); *Sherman v. Moore*, 86 F.R.D. 471, 473 (S.D.N.Y. 1980); *Fidan v. Austral Am. Trading Corp.*, 8 Misc. 2d 598, 600, 168 N.Y.S.2d 27, 30 (Sup. Ct. 1957). See also *Frontier Excavating, Inc. v. St. Paul Fire and Marine Ins. Co.*, 50 Misc. 2d 232, 233, 269 N.Y.S.2d 782, 783 (Sup. Ct. 1966); N.Y. CIV. PRAC. L. & R. 501 (McKinney 1976) (providing that "[s]ubject to the provisions of subdivision two of section 510, written agreement fixing place of trial, made before an action is commenced, shall be enforced upon a motion for change of place of trial.>").

<sup>18</sup> See *Neirbo*, 308 U.S. at 167; *Cooper v. Reynolds*, 77 U.S. 308, 316 (1870) ("By jurisdiction over the subject-matter is meant the nature of the cause of action and

courts are courts of limited subject matter jurisdiction, they are given a specific statutory grant of subject matter jurisdiction over civil actions against foreign states as to which foreign states do not have a defense of sovereign immunity.<sup>19</sup> Because sovereign immunity does not bar jurisdiction if the sovereign entity has waived its immunity,<sup>20</sup> and sovereign debt agreements invariably provide for waivers of immunity as to any actions arising thereunder, district courts will have the power to hear almost any action under a debt agreement against a foreign sovereign debtor.<sup>21</sup>

In contrast, although the courts of New York State have general subject matter jurisdiction, lack of subject matter jurisdiction provides at least a theoretical bar to the adjudication in New York state courts of certain disputes arising pursuant to sovereign debt agreements. The New York Business Corporation Law ("B.C.L.")<sup>22</sup> denies New York

of the relief sought; and this is conferred by the sovereign authority which organizes the court, and is to be sought for in the general nature of its powers, or in authority specially conferred."); *Reale Int'l, Inc. v. Federal Republic of Nigeria*, 647 F.2d 330, 331-32 (2d Cir. 1981); *Benson v. Eastern Bldg. & Loan Ass'n*, 174 N.Y. 83, 86, 66 N.E. 627, 628 (1903); *Fidan*, 8 Misc. 2d at 599, 168 N.Y.S.2d at 30.

<sup>19</sup> 28 U.S.C. § 1330(a) (1988).

<sup>20</sup> 28 U.S.C. § 1605(a)(1) (1988).

<sup>21</sup> For a more complete discussion of sovereign immunity to jurisdiction, see *infra* notes 137-41 and accompanying text.

<sup>22</sup> Section 1314(b) provides:

(b) Except as otherwise provided in this article, an action or special proceeding against a foreign corporation may be maintained by another foreign corporation of any type or kind or by a non-resident in the following cases only:

(1) Where it is brought to recover damages for the breach of a contract made or to be performed within this state, or relating to property situated within this state at the time of the making of the contract.

(2) Where the subject matter of the litigation is situated within this state.

(3) Where the cause of action arose within this state . . . .

(4) Where, in any case not included in the preceding subparagraphs, a non-domiciliary would be subject to the personal jurisdiction of the courts of this state under section 302 of the civil practice law and rules.

(5) Where the defendant is a foreign corporation doing business or authorized to do business in this state.

N.Y. BUS. CORP. LAW § 1314(b) (McKinney 1986).

Although section 1314 does not expressly limit New York state court subject matter jurisdiction in actions against foreign states themselves, it does limit jurisdiction over suits against foreign governmental corporations. These corporations would likely include the central bank of a foreign state (which is likely to be a borrower under, or guarantor of obligations incurred in, sovereign debt agreements). See Gruson, *Contractual Choice of Law and Choice of Forum: Unresolved Issues*, in JUDICIAL ENFORCEMENT OF INTERNATIONAL DEBT OBLIGATIONS 1, 39 (D. Sasson & D. Bradlow eds. 1987) (hereinafter Gruson, *Contractual Choice of Law and Choice of Forum*). See also N.Y. BANKING LAW § 200-b(2) (McKinney 1990) (containing provisions parallel to section 1314 with respect to actions by nonresidents against foreign banks).

state courts subject matter jurisdiction over actions by nonresidents<sup>23</sup> of New York State against foreign corporations, including foreign governmental corporations, unless the foreign corporation or the action itself bears some reasonable relationship to the state.<sup>24</sup> Thus, in some circumstances, parties to a contract might provide that New York law governs the agreement, and that any disputes arising under it are to be resolved by New York state courts, only to find that, pursuant to section 1314 of the B.C.L., such an action, to the extent it is against a foreign corporation, cannot be brought in those courts.

In 1984, the New York State legislature responded to concerns that existing New York law did not provide sufficient certainty for parties wishing to apply New York law to their agreements or to submit to the jurisdiction of New York courts by enacting new provisions which expanded the subject matter jurisdiction of New York courts to include certain previously barred actions. Newly enacted section 5-1401 of the New York General Obligations Law ("G.O.L.")<sup>25</sup> permits parties to make a binding decision that New York law will govern the agreement, as long as it relates to a transaction covering not less than two hundred fifty thousand dollars in the aggregate, even if the agreement bears no

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<sup>23</sup> A resident is deemed to include a domestic corporation or a foreign corporation authorized to transact business in the state. *Cf.* N.Y. CIV. PRAC. L. & R. 503(c) (McKinney 1976).

<sup>24</sup> Courts construing section 1314 have held it to be a restriction on subject matter jurisdiction. *See* *Farrell v. Piedmont Aviation, Inc.*, 411 F.2d 812, 815 n.4 (2d Cir. 1969), *cert. denied*, 396 U.S. 840 (1969); *Fidan v. Austral Am. Trading Corp.*, 8 Misc. 2d 598, 600, 168 N.Y.S.2d 27, 30-31 (Sup. Ct. 1957) (discussing section 225 of New York General Corporation Law, the predecessor of section 1314). This restriction reflects the New York policy against utilizing its courts for the resolution of disputes by nonresidents. *See id.* Thus, its limitations are mandatory upon the courts and cannot be waived by the parties. *Id.* ("It is jurisdictional and may be raised by a party affirmatively or by the court on its own motion at any time before judgment. If the action does not fall within the subdivisions of this section, the court must dismiss it.").

<sup>25</sup> Section 5-1401 provides:

1. The parties to any contract, agreement or undertaking, contingent or otherwise, in consideration of, or relating to any obligation arising out of a transaction covering in the aggregate not less than two hundred fifty thousand dollars, including a transaction otherwise covered by subsection one of section 1-105 of the uniform commercial code, may agree that the law of this state shall govern their rights and duties in whole or in part, whether or not such contract, agreement or undertaking bears a reasonable relation to this state. This section shall not apply to any contract, agreement or undertaking (a) for labor or personal services, (b) relating to any transaction for personal, family or household services, or (c) to the extent provided to the contrary in subsection two of section 1-105 of the uniform commercial code.
2. Nothing contained in this section shall be construed to limit or deny the enforcement of any provision respecting choice of law in any other contract, agreement or undertaking.

relationship to the state. Similarly, newly enacted G.O.L. section 5-1402<sup>26</sup> provides that an action under an agreement can be maintained in a New York state court where the parties to an agreement have stipulated, in accordance with section 5-1401, that New York law governs their agreement, and the agreement relates to a transaction covering not less than one million dollars in the aggregate and contains a submission of the parties to New York state court jurisdiction. Thus, where the jurisdictional amount, consent, and choice of law requirements of section 5-1402 are satisfied, a court no longer needs to determine whether one or more of the B.C.L. section 1314 bases of jurisdiction is present in order to establish subject matter jurisdiction over an action between a non-New York resident and a foreign corporation.<sup>27</sup>

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<sup>26</sup> Section 5-1402 provides:

1. Notwithstanding any act which limits or affects the right of a person to maintain an action or proceeding, including, but not limited to, paragraph (b) of section thirteen hundred fourteen of the business corporation law and subdivision two of section two hundred-b of the banking law, any person may maintain an action or proceeding against a foreign corporation, non-resident, or foreign state where the action or proceeding arises out of or relates to any contract, agreement or undertaking for which a choice of New York law has been made in whole or in part pursuant to section 5-1401 and which (a) is a contract, agreement or undertaking, contingent or otherwise, in consideration of, or relating to any obligation arising out of a transaction covering in the aggregate, not less than one million dollars, and (b) which contains a provision or provisions whereby such foreign corporation or non-resident agrees to submit to the jurisdiction of the courts of this state.
2. Nothing contained in this section shall be construed to affect the enforcement of any provision respecting choice of forum in any other contract, agreement or undertaking.

N.Y. GEN. OBLIG. LAW § 5-1402 (McKinney 1989).

This language contains a puzzling inconsistency. The first part of section 5-1402(1) allows any person to maintain an action against "a foreign corporation, non-resident, or foreign state" where the statutory conditions are met. N.Y. GEN. OBLIG. LAW § 5-1402(1) (McKinney 1989) (emphasis added). However, the latter part of section 5-1402(1), referring to the requirement of a contractual submission to New York's jurisdiction, states "and (b) which contains a provision or provisions whereby such foreign corporation or non-resident agrees to submit to the jurisdiction of the courts of this state." *Id.*

This inconsistency appears to have been mere oversight on the part of the statute's drafters. The legislative memorandum accompanying the bill notes that "it is assumed that the New York Courts will interpret the word 'non-resident' in Section 5-1402 liberally for purposes of Rule 327 to include foreign sovereigns and instrumentalities as well as foreign partnerships." *Memorandum of Assemblyman Mark Alan Siegal*, 1984 NEW YORK STATE LEGIS. ANN. 156, 157. In light of this language, it seems probable that the inclusion of the words "or foreign state" in the first part of section 5-1402 is a redundancy.

<sup>27</sup> In contrast, New York state courts will always have subject matter jurisdiction over an action by a New York resident against a foreign corporation, whether or not the action or the foreign corporation bears some reasonable relationship to the state. *See Jacobsen v. United States Shipping Bd. Emergency Fleet Corp.*, 128 Misc. 138, 140,

Even without the benefit of section 5-1402, however, a New York court will likely have subject matter jurisdiction over an action by a nonresident plaintiff seeking repayment of a debt by a foreign governmental corporation. In most sovereign debt agreements, at least one of the section 1314 bases for subject matter jurisdiction will probably be present, as the majority of such agreements are either "made" in New York or are to be performed in New York.<sup>28</sup> If, however, none of the section 1314 jurisdictional bases is present and the requirements of section 5-1402 are not satisfied, a contractual choice of a New York State court forum cannot be honored because the chosen court will lack subject matter jurisdiction. For example, where an agreement that relates to a transaction worth more than one million dollars bears no relationship to New York State (because it was negotiated outside New York by nonresidents and is not to be performed in the state) and specifies a New York State forum, but chooses another law to govern the transaction, New York State courts will lack the necessary statutory authorization to hear an action under the agreement.<sup>29</sup>

### 2.1.2. *Enforcement of Choice of Forum Clauses*

Even where a court has both personal and subject matter jurisdiction, and venue is proper, under some circumstances a court will refuse to hear an action. This situation is particularly likely when the agreement at issue contains a forum selection clause that provides for an exclusive choice of a different forum. The "enforceability" of a forum selection clause typically arises in one of several contexts. First, if an action is commenced in an excluded forum (i.e., a forum other than the

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217 N.Y.S. 856, 858 (Sup. Ct. 1926) (construing an earlier version of section 1314, the court noted that:

While . . . discretion exists [whether to hear] . . . actions by non-residents or foreign corporations against foreign corporations [where such suits were authorized by the statute], it does not exist in actions brought by residents or domestic corporations against foreign corporations. In the latter case the right of action is positive, and jurisdiction is compulsory, if properly obtained by the service of process.

(citations omitted)).

<sup>28</sup> N.Y. BUS. CORP. LAW § 1314(b)(1) (McKinney 1986). See *J. Zeevi & Sons, Ltd. v. Grindlays Bank (Uganda) Ltd.*, 37 N.Y.2d 220, 226-27, 333 N.E.2d 168, 172, 371 N.Y.S.2d 892, 897-98, (1975) *cert. denied*, 423 U.S. 866 (1975) (where New York was to be the place of payment of a letter of credit, and repudiation rather than payment was made in New York, the cause of action arose in New York for purposes of the jurisdictional statutes).

<sup>29</sup> See *Bank of Am. Nat'l Trust & Sav. Ass'n v. Envases Venezolanas, S.A.*, 740 F. Supp. 260, 264 (S.D.N.Y. 1990). In contrast, if the parties to such a transaction have chosen New York State law to govern, the forum selection clause will be enforceable by virtue of the section 5-1402 override of the jurisdictional restrictions of section 1314.

one designated as the exclusive forum in which litigation will be conducted), the issue of the enforceability of a forum selection clause will arise if the defendant moves to dismiss the action on the ground that the court should, as a matter of contract law, enforce the parties' selection of an exclusive forum for litigation. Second, a defendant in this situation may, additionally or alternatively, move to dismiss or stay the action in favor of the contractual forum under the doctrine of forum non conveniens.<sup>30</sup> Moreover, if the excluded forum is a federal court, the defendant may seek to transfer the action under 28 U.S.C. section 1404(a)<sup>31</sup> to a federal court authorized to hear the action pursuant to the forum selection clause. Third, even if the action is commenced in a forum permitted by the forum selection clause, a defendant may nonetheless move to stay or dismiss the action in favor of a more convenient forum in either a state or federal court under the doctrine of forum non conveniens or, if in a federal court, to transfer the action under 28 U.S.C. Section 1404(a). Although the issue of the enforceability of forum selection clauses typically arises in one of these three procedural postures, federal courts do not make precise analytical distinctions among them. As a result, it is impossible to derive any simple and reliable rules for the enforceability of such clauses that will be valid in all three settings.

#### (a) Specific Enforcement of Forum Selection Clauses

##### (i) The Federal Rule

When an action is commenced outside an exclusive forum, the first question before the court is whether the court will specifically enforce the forum selection clause and dismiss the action. The Supreme Court confronted precisely this issue in the seminal case of *Bremen v. Zapata Off-Shore Co.*,<sup>32</sup> where the defendant made a motion to dismiss a federal admiralty action brought in violation of an exclusive forum selection clause. The Court phrased the issue as "whether [the district court] should have exercised its jurisdiction to do more than give effect to the legitimate expectations of the parties, manifested in their freely negotiated agreement, by specifically enforcing the forum clause."<sup>33</sup> The

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<sup>30</sup> For a discussion of the doctrine of forum non conveniens, see *infra* notes 73-106 and accompanying text.

<sup>31</sup> 28 U.S.C. § 1404(a) (1988). Section 1404(a) provides: "For the convenience of parties and witnesses, in the interest of justice, a district court may transfer any civil action to any other district or division where it might have been brought." *Id.*

<sup>32</sup> 407 U.S. 1 (1972).

<sup>33</sup> *Id.* at 12.

Court held that under federal law, forum selection clauses "are prima facie valid and should be enforced unless enforcement is shown by the resisting party to be 'unreasonable' under the circumstances."<sup>34</sup>

Following *Bremen*, courts have declined to enforce forum selection clauses as unreasonable in essentially six situations: (1) where the clause was procured through fraud; (2) where the clause was procured through an abuse of bargaining power; (3) where the contractual forum was not impartial; (4) where a strong public policy of the forum would be violated by the law which would be applied in the contractual forum; (5) where a statute restricts the enforceability of the clause; and (6) where the contractual forum is "seriously inconvenient" for the trial of the action.<sup>35</sup>

The fraud and overreaching defenses to enforcement of a forum selection clause would generally not be available in actions between sophisticated parties to complex agreements. But even sovereign lending agreements are not always negotiated by parties of equal commercial experience and sophistication. Hence, it is possible that, in certain situ-

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<sup>34</sup> *Id.* at 10. Any discussion of the "enforcement" of forum selection clauses presents certain analytic difficulties. Courts often speak in terms of "enforcing" or "specifically enforcing" such a clause, which implies that the effect of the forum clause is a matter of substantive contract law. This same language is also used, however, in the course of a court's disposition of a motion to dismiss a case for forum non conveniens, or to transfer a case pursuant to section 1404(a), which most likely involves issues of procedural law. See *infra* notes 73-106 and accompanying text. Thus, it is often not clear whether a court enforces a forum selection clause as a matter of substantive or procedural law.

In fact, in *Bremen*, the Court speaks of specific enforcement. 407 U.S. at 12, 15. Yet the case arose on the defendant's forum non conveniens motion to dismiss the case in favor of the contractual forum. Because *Bremen* was an admiralty case, this procedure/substance distinction was of little importance. Federal courts having admiralty jurisdiction apply federal law to questions of both substance and procedure. However, the distinction can be critical. In some circumstances, federal courts apply federal law to procedural questions, but are bound to apply the substantive law of the state in which they sit. See *infra* notes 73-106 and accompanying text.

The confusion is well illustrated by *Manetti-Farrow, Inc. v. Gucci Am., Inc.*, 858 F.2d 509, 512-13 (9th Cir. 1988), where the court granted a motion to dismiss the case on the basis of a forum selection clause which designated an alternate exclusive forum. Although the court spoke of specific enforcement of that clause, it granted the dismissal as a matter of federal procedural law. Indeed, since *Manetti-Farrow* was a diversity action, the court only could have applied federal law to the question by first finding that it was an issue of procedure. See *infra* notes 73-106 and accompanying text.

<sup>35</sup> Gruson, *Controlling Site of Litigation*, *supra* note 11, at 33. The *Bremen* rule has provided the standard both for motions to specifically enforce a forum selection clause and for motions to dismiss a case involving a forum selection clause for forum non conveniens. Thus, these factors will be relevant in both contexts. See *infra* notes 73-106 and accompanying text. See *Shute v. Carnival Cruise Lines*, 897 F.2d 377 (9th Cir. 1990), *cert. granted*, 111 S. Ct. 39 (1990) (under *Bremen*, the court refused to enforce the forum selection clause on two independent grounds: disparity in bargaining power and grave inconvenience).

ations, a sovereign borrower might plausibly claim that its agreement to an unfavorable forum selection clause was induced by fraud or overwhelmingly unequal bargaining power.<sup>36</sup>

In some instances, statutory restrictions on the freedom of parties to choose a forum may prevent courts from enforcing a forum selection clause. Although New York places few restraints on the parties' right to select a New York forum,<sup>37</sup> B.C.L. section 1314 may deprive New York courts of subject matter jurisdiction over certain actions, thereby precluding enforcement of a forum selection clause.<sup>38</sup>

"Serious inconvenience," as used by the *Bremen* Court,<sup>39</sup> is a term of art: to abrogate a forum selection clause on the basis of inconvenience to the parties, litigation in the contractual forum must be so gravely inconvenient to the resisting party that it will be essentially deprived of a meaningful day in court.<sup>40</sup> This is a much higher level of inconvenience than would be necessary to justify a transfer under the traditional forum non conveniens doctrine.<sup>41</sup> In the absence of a forum selection clause, the Supreme Court has held that dismissal on the ground of forum non conveniens would be appropriate where another forum would have jurisdiction to hear the case, and where the inconvenience of the chosen forum to the defendant substantially outweighs the convenience to the plaintiff.<sup>42</sup> But where an agreement contains a forum selection clause, any inconvenience to the parties should be foreseeable, and, indeed, bargained over at the time of contracting. Under these circumstances, the inconvenience must surpass what the parties

<sup>36</sup> In at least one case, a federal court has held that where a sovereign defendant had no meaningful opportunity to negotiate a consent-to-jurisdiction clause, it could not be bound by that clause. See *L'Europeenne de Banque v. La Republica de Venezuela*, 700 F. Supp. 114, 123 (S.D.N.Y. 1988).

<sup>37</sup> See Gruson, *Controlling Site of Litigation*, *supra* note 11, at 35.

<sup>38</sup> See *supra* notes 21-23 and accompanying text. See also *L'Europeenne de Banque*, 700 F. Supp. at 123 (court noted that it would have lacked subject matter jurisdiction in an action between the original parties to an international lending agreement, and therefore the forum selection clause designating that court as the forum for litigation would have been unenforceable in such an action).

Even law which is not jurisdictional in nature may occasionally have a similar effect. *E.g.*, *Behring Int'l Inc. v. Imperial Iranian Air Force*, 699 F.2d 657, 662-63 (3d Cir. 1983), *reh'g denied*, 712 F.2d 45 (3d Cir. 1983) (the court held that Executive Order No. 12294, which provided a mechanism for resolution of all disputes between American citizens and the new Iranian government as part of the settlement of the Iran hostage crisis, rendered unenforceable a choice of forum clause in an agreement between a U.S. company and an Iranian agency).

<sup>39</sup> 407 U.S. 1 at 17.

<sup>40</sup> *Id.* at 18-19. See *Shute*, 897 F.2d at 389.

<sup>41</sup> For a discussion of the doctrine of forum non conveniens, see *infra* notes 73-106 and accompanying text.

<sup>42</sup> See *Piper Aircraft Co. v. Reyno*, 454 U.S. 235, 241 (1981), *reh'g denied*, 455 U.S. 928 (1982); *Gulf Oil Corp. v. Gilbert*, 330 U.S. 501, 508-09 (1947).

could reasonably have foreseen to justify a refusal to enforce the parties' bargain.<sup>43</sup>

Finally, in determining the enforceability of a forum selection clause, the neutrality of the contractual forum and any important public policy of the forum where the action is pending that would be violated by the law to be applied in the contractual forum will be relevant. The neutrality of a selected forum has, however, rarely been questioned by New York courts in the years since it was first raised as a factor in *Bremen*.<sup>44</sup>

Although the *Bremen* court implied that absence of neutrality could be a basis for a court's refusal to enforce a forum selection clause, it cautioned courts against taking "a provincial attitude regarding the fairness of other tribunals."<sup>45</sup> Nonetheless, in sovereign lending agreements, this neutrality factor may, in rare instances, assume some importance. In the unlikely event that lenders have agreed to the sovereign borrower's courts as the exclusive forum, it is possible that United States courts might refuse to enforce the parties' choice on the ground that the chosen forum lacks neutrality.

The Supreme Court noted in *Bremen* that "[a] contractual choice-of-forum clause should be held unenforceable if enforcement would contravene a strong public policy of the forum in which suit is brought. . . ."<sup>46</sup> Such public policy concerns normally arise in connection with differences in the substantive law that would be applied in the competing fora.<sup>47</sup> One potential situation exists, however, in which the *Bremen* rule might have a different application in FSIA cases than in other cases. Although a forum's public policy would not normally prevent a court from accepting a case and applying that forum's law, such public policy concerns may be implicated when a non-United States citizen brings suit against a foreign sovereign in a United States court.<sup>48</sup> Therefore, it is possible that in a loan transaction that does not involve American parties and that is not related to the United States, a motion to dismiss for forum non conveniens may be granted, despite a contractual selection of a New York court.<sup>49</sup>

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<sup>43</sup> *Bremen*, 407 U.S. at 16-18.

<sup>44</sup> *Id.* at 12. See Gruson, *Controlling Site of Litigation*, *supra* note 11, at 44-45.

<sup>45</sup> *Bremen*, 407 U.S. at 12.

<sup>46</sup> *Id.* at 15.

<sup>47</sup> See, e.g., *Indussa Corp. v. S.S. Ranborg*, 377 F.2d 200, 204 (2d Cir. 1967) (the court invalidated the forum selection clause because United States law would have invalidated a certain contract clause and the law that would have been applied in the contractual forum would have upheld that clause).

<sup>48</sup> See *infra* note 80 and accompanying text.

<sup>49</sup> See *id.*

## (ii) The New York Rule

In connection with the enactment of G.O.L. sections 5-1401 and 5-1402,<sup>50</sup> the New York State legislature enacted New York Civil Practice Law and Rules ("C.P.L.R.") 327(b),<sup>51</sup> which limits a New York state court's discretion to dismiss or stay an action brought under an agreement containing a New York forum selection clause. Under this provision, a New York state court is prohibited from staying or dismissing an action on the ground of forum non conveniens "where the action arises out of or related to a contract, agreement or undertaking" which conforms to the requirements of Section 5-1402.<sup>52</sup> These requirements are satisfied by any agreement which stipulates that New York law will govern the agreement, designates New York state courts as a forum, and relates to a transaction covering not less than one million dollars in the aggregate.

Thus, where an agreement relating to a transaction covering not less than one million dollars calls for application of New York law in a New York forum, a New York state court, in theory, may no longer dismiss the action, even in extreme circumstances.<sup>53</sup> In contrast, in the rare case where an agreement specifies a New York state court as a forum but designates another governing law, a defendant faced with an action in New York state courts may be able to persuade the court to dismiss or stay the action.

This strict enforcement of forum selection clauses in the New York state court system may, however, be of limited importance to foreign sovereign defendants. Even if a sovereign debt agreement specifies the

<sup>50</sup> N.Y. GEN. OBLIG. LAW § 5-1402 (McKinney 1989).

<sup>51</sup> New York C.P.L.R. 327(b) provides:

Notwithstanding the provisions of subdivision (a) of this rule, the court shall not stay or dismiss any action on the ground of inconvenient forum, where the action arises out of or relates to a contract, agreement or undertaking to which section 5-1402 of the general obligations law applies, and the parties to the contract have agreed that the law of this state shall govern their rights or duties in whole or in part.

N.Y. CIV. PRAC. L. & R. 327(b) (McKinney 1990).

<sup>52</sup> *Id.* New York C.P.L.R. 327(a) codifies the New York doctrine of forum non conveniens as follows:

When the court finds that in the interest of substantial justice the action should be heard in another forum, the court, on the motion of any party, may stay or dismiss the action in whole or in part on any conditions that may be just. The domicile or residence in this state of any party to the action shall not preclude the court from staying or dismissing the action.

N.Y. CIV. PRAC. L. & R. 327(a) (McKinney 1990).

<sup>53</sup> See *infra* note 117 and accompanying text for a discussion of whether public policy concerns may override New York G.O.L. section 5-1402 and New York C.P.L.R. 327(b).

courts of New York State as the *exclusive* forum for the resolution of disputes, and that choice of forum is enforceable under New York law, a sovereign defendant may be able to remove the action to the appropriate federal district court. The FSIA "guarantees foreign states the right to remove any civil action from a state court to a federal court."<sup>54</sup> Although the Court of Appeals for the Sixth Circuit has held that a foreign state can waive its right of removal if it does so in "clear and unequivocal [terms],"<sup>55</sup> the Court of Appeals for the Second Circuit has not addressed this question.<sup>56</sup> In view of the FSIA's preference for the adjudication of actions against foreign sovereigns in federal court,<sup>57</sup> and of the FSIA's structure (which makes explicit provision for waivers of sovereign immunity and for agreements as to effective methods of service, but which makes no comparable provision for waiver of the right of removal), there is reason to believe that a sovereign defendant should not be able to waive the right to remove an action from state to federal court.<sup>58</sup>

### (iii) The Law Applicable to FSIA Cases

Where a federal court has jurisdiction under the FSIA by virtue of a defendant's status as a foreign state, it is not settled whether a court will apply federal law or the law of the forum in which it sits (e.g., New York) when ruling upon the enforceability of forum selection clauses. In cases where the jurisdiction of a federal court is founded solely on diversity of citizenship of the parties,<sup>59</sup> a federal court must

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<sup>54</sup> *Verlinden B.V. v. Central Bank of Nigeria*, 461 U.S. 480, 489 (1983). See 28 U.S.C. § 1441(d) (1988).

<sup>55</sup> *In re Delta Am. Re Ins. Co.*, 900 F.2d 890, 892 (6th Cir. 1990).

<sup>56</sup> *Refco, Inc. v. Abdul Wahab Bin Ebrahim Galadari & A.W. Galadari Commodities*, No. 90 Civ. 1240 (S.D.N.Y. Jan. 4, 1991) (LEXIS, Genfed Library, Dist. file). Though no forum selection clause was at issue, the court noted with approval authorities that suggested that a foreign state could not waive its right of removal under the FSIA.

<sup>57</sup> H.R. REP. NO. 1487, 94th Cong., 2d Sess. 32, reprinted in 1976 U.S. CODE CONG. & ADMIN. NEWS 6604, 6631.

<sup>58</sup> 14A C. WRIGHT, A. MILLER & E. COOPER, FEDERAL PRACTICE & PROCEDURE § 3729, (Supp. 1985). See also *Proyecfin de Venezuela, S.A. v. Banco Industrial de Venezuela, S.A.*, 760 F.2d 390, 396-97 (2d Cir. 1985) (While reserving the question of whether a sovereign defendant could waive the right of removal, the court emphasized that the strong federal policy of channeling litigation against sovereign defendants away from the state courts and into the federal courts supported a broad reading of the right to remove. The court refused to find an express or implied waiver of that right through contractual consent to jurisdiction.). But see *Karl Koch Erecting Co. v. New York Convention Center Dev. Corp.*, 838 F.2d 656, 659 (2d Cir. 1988) (exclusive state forum selection clause in non-FSIA case constitutes waiver of right of removal).

<sup>59</sup> Diversity of citizenship provides a basis for federal jurisdiction where certain statutory requirements are met. The diversity statute, 28 U.S.C. section 1332, states:

follow the substantive law of the state in which it sits, but will decide questions of procedure according to federal law.<sup>60</sup> In suits against a foreign sovereign, however, the FSIA provides the sole basis for jurisdiction.<sup>61</sup> Therefore, all such actions are federal question cases in which the courts are not constitutionally bound to apply the substantive law of the state in which they sit.<sup>62</sup> Nevertheless, while the Constitution does not require the application of state law in federal question cases, some statutory grants of federal question jurisdiction have been held to require the federal courts to look to state substantive law for their rules of decision.<sup>63</sup>

Consequently, the question of whether federal courts will determine the enforceability of a forum selection clause under state or federal law depends upon two separate determinations. If the enforceability of the clause is determined to be a question of procedure, the court will apply federal law. If enforceability is considered a question of substance, however, the court must then determine whether Congress intended the courts to apply state substantive law in FSIA cases, and will apply state or federal law based on its understanding of Congress' intent.<sup>64</sup>

The federal courts of appeals have split on whether the enforceability of a forum selection clause<sup>65</sup> is a matter of substance, possibly

(a) The district courts shall have original jurisdiction of all civil actions where the matter in controversy exceeds the sum or value of \$50,000, exclusive of interest and costs, and is between —

- (1) citizens of different States;
- (2) citizens of a State and citizens or subjects of a foreign state;
- (3) citizens of different States and in which citizens or subjects of a foreign state are additional parties; and
- (4) a foreign state, defined in section 1603(a) of this title, as plaintiff and citizens of a State or of different States.

28 U.S.C. § 1332 (1988).

<sup>60</sup> *Klaxon Co. v. Stentor Elec. Mfg. Co.*, 313 U.S. 487 (1941); *Erie R.R. v. Tompkins*, 304 U.S. 64 (1938).

<sup>61</sup> *Argentine Republic v. Amerada Hess Shipping Corp.*, 488 U.S. 428 (1989); *Verlinden B.V. v. Central Bank of Nigeria*, 461 U.S. 480, 489 (1983); *Ruggiero v. Compania Peruana de Vapores "Inca Capac Yupanqui"*, 639 F.2d 872, 875 (2d Cir. 1981).

<sup>62</sup> *See Corporacion Venezolana de Fomento v. Vintero Sales Corp.*, 629 F.2d 786 (2d Cir. 1980), *cert. denied*, 449 U.S. 1080 (1981) (federal question jurisdiction arising under the Edge Act).

<sup>63</sup> *See First Nat'l City Bank v. Banco Para el Comercio Exterior de Cuba*, 462 U.S. 611, 622 n.11 (1983) (dictum comparing FSIA and Federal Tort Claims Act).

<sup>64</sup> If the court applies state law, it must then determine whether to apply that state's "whole" law, or merely its substantive law.

<sup>65</sup> This issue arises again in a slightly different form when a party tests the enforceability of a forum selection clause by a motion to dismiss for *forum non conveniens* in federal court. In analyzing whether such a motion is to be decided as a matter of procedural or of substantive law, some courts, such as *Manetti-Farrow, Inc. v. Gucci*

governed by state law,<sup>66</sup> or procedure, governed by federal law.<sup>67</sup> The Supreme Court has not yet decided the issue.

(b) Transfers of Federal Court Actions Pursuant to Section 1404

Under 28 U.S.C. section 1404(a), a party can seek to transfer a case from one federal court to another “[f]or the convenience of the parties and witnesses [and] in the interest of justice.”<sup>68</sup> In *Stewart Organization, Inc. v. Ricoh Corp.*,<sup>69</sup> the Supreme Court held that a mo-

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America, Inc., 858 F.2d 509 (9th Cir. 1988), speak of whether the enforceability of a forum selection clause is a matter of substantive or procedural law. Other courts speak of whether the particular testing mechanism, such as 28 U.S.C. section 1404(a) or forum non conveniens, is substantive or procedural. Therefore, it is not certain whether a court's holding that the enforceability of a forum selection clause is a matter of procedural law, should be interpreted to mean that all the devices by which that enforceability may be tested raise questions of procedure, or whether the court is referring only to the device at issue in the case. See, e.g., *Alexander Proudfoot Co. v. Thayer*, 877 F.2d 912, 918-19 (11th Cir. 1989) (where the court held that a motion to dismiss on grounds of a forum selection clause is substantive and must be decided under state law, even though, after *Ricoh*, a motion to transfer the case under 28 U.S.C. section 1404(a) grounded upon a forum clause would clearly be a procedural issue governed by federal law). See *In re Ricoh Corp.*, 870 F.2d 570 (11th Cir. 1989), *on reh'g*, *Stewart Organization, Inc. v. Ricoh Corp.*, 487 U.S. 22 (1988).

<sup>66</sup> The Third Circuit has held that the enforceability of a forum selection clause is a question of substantive law that must, in a diversity action, be determined under state law. *General Eng'g Corp. v. Martin Marietta Alumina, Inc.*, 783 F.2d 352, 356-57 (3d Cir. 1986). The Eleventh Circuit's position is somewhat unclear. In *In re Ricoh Corp.*, the court on remand analyzed the petitioner's motion to transfer venue to the selected forum under 28 U.S.C. section 1404(a), and concluded that federal law required that the forum clause be enforced and the transfer granted. 870 F.2d 570. In *Alexander Proudfoot Co.*, 877 F.2d at 912, however, the court considered a defendant's motion to dismiss for lack of personal jurisdiction an action brought in the contractual forum, and concluded that the effect of the forum selection clause was a substantive matter that must be analyzed under state law. It thus appears that the Eleventh Circuit has adopted a rule that would treat issues of venue raised under a forum selection clause as procedural matters governed by federal law, but would treat issues of jurisdiction raised under an identical forum clause as substantive questions requiring the application of state law.

<sup>67</sup> The Courts of Appeals for the Second and Ninth Circuits have held that forum selection clauses are procedural and, therefore, their enforceability in federal courts should be decided under federal law. *Jones v. Weibrecht*, 901 F.2d 17, 18 (2d Cir. 1990); *Manetti-Farrow*, 858 F.2d at 512-13; *Karl Koch Erecting Co. v. New York Convention Center Dev. Corp.*, 838 F.2d 656, 659 (2d Cir. 1988) (diversity action); *Luce v. Edelstein*, 802 F.2d 49, 57 (2d Cir. 1986) (motion to dismiss pendent state claims); *TUC Elecs., Inc. v. Eagle Telephonics, Inc.*, 698 F. Supp. 35, 37-38 (D. Conn. 1988) (diversity action); *Richardson Greenshields Sec., Inc. v. Metz*, 566 F. Supp. 131 (S.D.N.Y. 1983) (diversity action). As noted in note 66, *supra*, the Eleventh Circuit has taken an ambiguous position on the question. The Court of Appeals for the Seventh Circuit has noted in dicta that the validity of a forum selection clause is governed by federal law. *Northwestern Nat'l Ins. Co. v. Donovan*, 916 F.2d 372, 374 (7th Cir. 1990).

<sup>68</sup> 28 U.S.C. § 1404(a) (1990).

<sup>69</sup> 487 U.S. 22 (1988), *on remand sub nom. In re Ricoh Corp.*, 870 F.2d 570

tion to transfer a case pursuant to section 1404(a) from an excluded federal court to an exclusive contractual forum must be decided under federal law, even in a diversity action (where state law provides the substantive rules of decision).<sup>70</sup> Under section 1404(a), a court must weigh such factors as the convenience of witnesses and the allocation of the burdens of litigation between the parties. In this analysis, the presence of a forum selection clause will be a significant, but not a dispositive, factor.<sup>71</sup>

As a result, in the unlikely event that it is considerably more convenient to try an action under a sovereign debt agreement which selects a federal court sitting within New York as the contractual forum in a federal court sitting outside of New York, a federal court could order a transfer despite the forum selection clause. Moreover, where a sovereign debt agreement selects both the courts of New York States as the exclusive forum and New York law to govern the agreement, a sovereign defendant sued in state court may nevertheless be able to remove the action to federal court and obtain a section 1404(a) transfer, even though the New York state courts would have no discretion to stay or dismiss the action. A transfer under section 1404(a) will not change the governing law. The transferee court will apply the same law that the transferor court would have employed to decide the case.<sup>72</sup>

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(11th Cir. 1989).

<sup>70</sup> The *Ricoh* holding is based on the supremacy of federal statutory law over state law, and the Court emphasized that the enactment of the statute was indicative of Congressional intent that transfer motions be considered under the standards set forth in the statute, rather than under any state rules. *Ricoh*, 487 U.S. at 31. The Court goes on to note that section 1404(a) is procedural in character. *Id.* at 31. From the Court's reasoning, it is not clear, however, what law the Court would have applied had the defendant made a motion specifically to enforce the forum selection clause and dismiss the action rather than transfer it. Therefore, *Ricoh* does not shed any new light on the split among the circuits as to whether enforcement of a forum selection clause is procedural or substantive in nature. See *supra* notes 65-67 and accompanying text.

<sup>71</sup> *Ricoh*, 487 U.S. at 29-31. The existence of a forum selection clause shifts the burden of persuasion to the party opposing enforcement of that clause. *Ricoh*, 870 F.2d 570 (11th Cir. 1989).

<sup>72</sup> *Ferens v. John Deere Co.*, 110 S. Ct. 1274 (1990); *Van Dusen v. Barrack*, 376 U.S. 612 (1964).

The problems of whether enforcement of a forum selection clause is considered a matter of procedural or substantive law may be of decisive importance. If suit is brought in violation of an exclusive forum selection clause in the Third Circuit, which considers the enforcement of forum clauses a question of substantive contract law, presumably a defendant could remove the case to federal court and then seek a transfer to the contractual forum. See *General Eng'g Corp. v. Martin Marietta Alumina, Inc.*, 783 F.2d 352, 356-57 (3d Cir. 1986). See *supra* notes 54-58 and accompanying text. However, if the defendant asks the federal court specifically to enforce the clause by dismissing the action, the court will be presented with a question of substantive law and may look to the law of the state in which it sits. See *supra* notes 59-67 and accompanying text. If that state does not enforce forum selection clauses, the court could deny the

## (c) Forum Non Conveniens

Under the doctrine of forum non conveniens, a state or federal court can stay or dismiss an action, notwithstanding a forum selection clause, when to do so would be "in the interest of substantial justice." The New York Court of Appeals (the highest New York state court) explained the doctrine of forum non conveniens as follows:

The burden rests upon the defendant challenging the forum to demonstrate relevant private or public interest factors which militate against accepting the litigation, and the court, after considering and balancing the various competing factors, must determine in the exercise of its sound discretion whether to retain jurisdiction or not. Among the factors to be considered are the burden on the New York courts, the potential hardship to the defendant, and the unavailability of an alternative forum in which the plaintiff may bring suit. The court may also consider that both parties to the action are nonresidents and that the transaction out of which the cause of action arose occurred primarily in a foreign jurisdiction. No one factor is controlling. The great advantage of the rule of forum non conveniens is its flexibility based upon the facts and circumstances of each case.<sup>73</sup>

Under C.P.L.R. 327(a), a New York state court may, on a party's motion, stay or dismiss an action which, although jurisdictionally sound, would "in the interest of substantial justice" be better adjudicated elsewhere.<sup>74</sup> New York courts hold, however, that in an action pursuant to a contract that contains a clause selecting New York as the forum, the court's discretion should normally be exercised in favor of retaining jurisdiction.<sup>75</sup> For example, in *Credit Francais International S.A. v. Sociedad Financiera de Comercio, C.A.*,<sup>76</sup> the court declined to dismiss a dispute between two nonresidents, a French bank and a Ven-

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motion to dismiss, even though a transfer may have been available on identical facts under section 1404(a).

<sup>73</sup> *Islamic Republic of Iran v. Pahlavi*, 62 N.Y.2d 474, 479, 467 N.E.2d 245, 247-48, 478 N.Y.S.2d 597, 599-600 (1984), cert. denied, 469 U.S. 1108 (1985) (citations omitted). The New York Court of Appeals is the highest state court in New York.

<sup>74</sup> N.Y. CIV. PRAC. L. & R. 327(a) (McKinney 1990). For the text of the entire rule, see *supra* note 52.

<sup>75</sup> *Triad Fin. Establishment v. Tumpene Co.*, 611 F. Supp. 157, 162 (N.D.N.Y. 1985); *Arthur Young & Co. v. Leong*, 53 A.D.2d 515, 516, 383 N.Y.S.2d 618, 619 (1976), appeal dismissed, 40 N.Y.2d 984, 359 N.E.2d 435, 390 N.Y.S.2d 927 (1976); *Credit Francais Int'l, S.A. v. Sociedad Financiera de Comercio, C.A.*, 128 Misc. 2d 564, 570, 490 N.Y.S.2d 670, 676 (Sup. Ct. 1985).

<sup>76</sup> 128 Misc. 2d at 568, 490 N.Y.S.2d at 674.

ezuelan financial institution, that resulted from an international loan agreement that stipulated that New York law would govern and that any dispute under the agreement could be adjudicated in New York state or federal courts.<sup>77</sup>

Since 1984, the outcome of forum non conveniens motions in New York Courts in proceedings based upon contracts differs according to whether the parties have chosen New York law to govern their agreement and whether section 5-1402<sup>78</sup> is applicable. As noted above, when section 5-1402 is satisfied, the court no longer has the discretion to choose whether or not to enforce the forum selection clause. In other cases, the New York courts will presumably continue to follow the rule of *Bremen*.<sup>79</sup>

Dismissal for forum non conveniens is also available under appropriate circumstances in FSIA cases in the federal courts.<sup>80</sup> The Supreme Court has yet to resolve the general question of whether forum non conveniens, when raised in the federal courts, is a procedural matter to which federal law applies, or a substantive matter which may

<sup>77</sup> Although *Credit Francais* was decided in 1985, the action was commenced before the passage of G.O.L. sections 5-1401 and 5-1402. N.Y. GEN. OBLIG. LAW §§ 5-1401, 5-1402 (McKinney 1989). Therefore, the case was not decided under the new statutory provisions, although the court cited them as evidence of New York's policy of upholding parties' choice of New York law and of a New York forum.

<sup>78</sup> *Id.* at § 5-1402.

<sup>79</sup> 407 U.S. 1 (1972). The *Bremen* standard has been applied by New York state courts as the New York rule for the enforceability of forum selection agreements. See *National Union Fire Ins. Co. v. Weir*, 131 A.D.2d 380, 381, 517 N.Y.S.2d 141, 142 (1987); *Rokeby-Johnson v. Kentucky Agric. Energy Corp.*, 108 A.D.2d 336, 339-41, 489 N.Y.S.2d 69, 72-74 (1985); *Arthur Young*, 53 A.D.2d at 516, 383 N.Y.S.2d at 619; *Credit Francais*, 128 Misc. 2d at 568, 490 N.Y.S.2d at 674.

<sup>80</sup> The Supreme Court has stated in dictum that the FSIA leaves traditional forum non conveniens doctrine in place. *Verlinden B.V. v. Central Bank of Virginia*, 461 U.S. 480, 490 n.15 (1983). See also *Proyecfin de Venezuela, S.A. v. Banco Industrial de Venezuela, S.A.*, 760 F.2d 390, 394 (2d Cir. 1985).

Dismissal of an FSIA action on the grounds of forum non conveniens may be available when the dispute is between non-United States parties and bears no substantial relationship to the United States. As reflected in the FSIA's legislative history, Congress was concerned that the courts of the United States might be indiscriminately used for every dispute between a foreign plaintiff and a foreign sovereign. Rather than restrict the class of potential plaintiffs under the FSIA, Congress generally limited the class of actions that might be brought thereunder to those with "some form of substantial contact with the United States." *Verlinden* at 490. The Supreme Court has noted that the FSIA's grant of jurisdiction whenever a foreign sovereign has waived its immunity is an exception to the general requirement of substantial contact with the United States. The Court suggested that, in the absence of any other contact with the United States, such a suit brought in the United States courts might be dismissed for forum non conveniens. *Id.* at 490 n.15.

Thus, under certain circumstances, in an action under the FSIA, a dismissal for forum non conveniens might be proper under federal law, even though it might be improper in a New York state court under C.P.L.R. 327(b).

require the application of state law.<sup>81</sup> Similarly, the Second Circuit has not definitively resolved the question. In *Weiss v. Reuth*,<sup>82</sup> the Court of Appeals for the Second Circuit held that federal courts should apply state law to the question. However, the following year, in *Gilbert v. Gulf Oil Corp.*,<sup>83</sup> a different panel of the same court held that the federal courts were not bound to follow the state rule. Since those decisions, rendered more than forty years ago, some federal courts, when confronted with the issue, have noted that the question remains unresolved.<sup>84</sup> Others have held that forum non conveniens presents issues of procedural law and therefore should be resolved according to federal rules.<sup>85</sup> Many of these courts rest their reasoning either upon the proposition that forum non conveniens is identical to section 1404(a) in the federal courts,<sup>86</sup> or upon cases that were decided under section 1404(a).<sup>87</sup> Therefore, while these courts may reach the proper result, it is doubtful, in light of *Ricoh*,<sup>88</sup> that their analysis of the issue can be considered correct. In recent cases, federal courts in New York have generally applied federal law to forum non conveniens motions without discussion.<sup>89</sup>

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<sup>81</sup> See *Piper Aircraft Co. v. Reyno*, 454 U.S. 235, 248 n.13 (1981), *reh'g denied*, 455 U.S. 928 (1982); *Gulf Oil Corp. v. Gilbert*, 330 U.S. 501, 509 (1947) (reserving judgment on whether New York State or federal standards were controlling, as they were substantially the same).

<sup>82</sup> 149 F.2d 193 (2d Cir. 1945).

<sup>83</sup> 153 F.2d 883 (2d Cir. 1946), *rev'd on other grounds*, 330 U.S. 501 (1947).

<sup>84</sup> *Thomson v. Palmieri*, 355 F.2d 64, 66 (2d Cir. 1966); *Burton v. Exxon Corp.*, 536 F. Supp. 617, 625 n.11 (S.D.N.Y. 1982).

<sup>85</sup> *Ciprari v. Servicos Aereos Cruzeiro do Sul, S.A.*, 232 F. Supp. 433, 442 (S.D.N.Y. 1964); *Shulman v. Compagnie Generale Transatlantique*, 152 F. Supp. 833, 835 (S.D.N.Y. 1957). See also *Hodson v. A.H. Robins Co.*, 528 F. Supp. 809, 817 (E.D. Va. 1981), *aff'd*, 715 F.2d 142 (4th Cir. 1983) (citing *Fiorenza v. United States Steel Int'l, Ltd.*, 311 F. Supp. 117, 119 (S.D.N.Y. 1969) for the proposition that forum non conveniens is governed by federal law in a federal court).

<sup>86</sup> *Willis v. Weil Pump Co.*, 222 F.2d 261 (2d Cir. 1955); *Ultra Sucro Co. v. Illinois Water Treatment Co.*, 146 F. Supp. 393, 396 (S.D.N.Y. 1956).

<sup>87</sup> *Ciprari*, 232 F. Supp. at 442.

<sup>88</sup> 487 U.S. 22 (1988).

<sup>89</sup> *In re Union Carbide Corp. Gas Plant Disaster at Bhopal, India in Dec., 1984*, 809 F.2d 195, 198, 202 (2d Cir. 1987), *cert. denied*, 484 U.S. 871 (1987); *Chhawchharia v. Boeing Co.*, 657 F. Supp. 1157, 1159-62 (S.D.N.Y. 1987). See also *Intel Corp. v. Malaysian Airline Sys.*, 652 F. Supp. 1101, 1103 (N.D. Cal. 1987) (court implicitly applied federal law standards to the forum non conveniens inquiry, but noted that it would apply the choice of law rules of the transferor state); 1A J. MOORE, W. TAGGART, A. VESTAL, J. WICKER & B. RINGLE, *MOORE'S FEDERAL PRACTICE* ¶ 0.317[2] (2d ed. 1989) [hereinafter *MOORE'S FEDERAL PRACTICE*] ("[The federal courts] should be independent of state doctrines of forum non conveniens, fashioned for courts operating on a state scale. Forum non conveniens is procedural. . . . *Erie R. Co. v. Tompkins* [sic] does not require conformity by the federal courts to the practice of the states in this matter.") (citations omitted).

The Supreme Court's recent holding in *Ricoh*,<sup>90</sup> although not based on conflicts of law principles, may be an indication that forum non conveniens motions in federal court should be decided under federal law as a matter of procedural law, rather than as a matter of state substantive law.<sup>91</sup> Forum non conveniens and transfer of venue pursuant to section 1404(a) are analogous doctrines<sup>92</sup> allowing for the shifting of the venue of an action to a more convenient forum, even though jurisdiction and venue were proper in the original court.<sup>93</sup> Section 1404(a) permits a court to transfer an action to another court in the federal system, while forum non conveniens allows a court to dismiss an action which should be brought in another forum when the court lacks the power to transfer the case to that forum. (Presumably, after such dismissal the plaintiff would recommence its suit in the appropriate forum, thus completing the "transfer.") Since the two doctrines serve essentially the same purpose and are generally governed by the same considerations, it would be illogical for the courts to decide section 1404(a) motions under federal law, but to decide forum non conveniens motions under state law.<sup>94</sup>

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<sup>90</sup> 487 U.S. at 28-32.

<sup>91</sup> At least one lower court has so interpreted the *Ricoh* holding. See, e.g., TUC Elecs., Inc. v. Eagle Telephonics, Inc., 698 F. Supp. 35, 37-38 (D. Conn. 1988).

<sup>92</sup> Congress drafted section 1404(a) with reference to the rules governing forum non conveniens. Piper Aircraft Co. v. Reyno, 454 U.S. 235, 253 (1981), *reh'g denied*, 455 U.S. 928 (1982) (citing Revisor's note, H.R. REP. NO. 308, 80th Cong., 1st Sess., A132 (1947); H.R. REP. NO. 2646, 79th Cong., 2d Sess., A127 (1946)). A court, however, has broader discretion with respect to a section 1404(a) transfer motion than it has with respect to a forum non conveniens motion. This discretion reflects the fact that the result of granting the section 1404(a) motion is less harsh; it does not end the action or alter the governing law, but merely shifts the action to another location. In contrast, granting a forum non conveniens motion puts an end to the litigation. See *id.*; Norwood v. Kirkpatrick, 349 U.S. 29, 31-32 (1955).

<sup>93</sup> See 1A MOORE'S FEDERAL PRACTICE, *supra* note 89, at ¶ 0.317[2]. ("[F]orum non conveniens is but an aspect of venue.").

<sup>94</sup> Nevertheless, it should be noted that forum non conveniens differs from a section 1404(a) transfer in at least one important respect. When a case is transferred under section 1404(a), the transferee court decides the case under the same law that the transferor court would have applied. *Ricoh*, 487 U.S. 22. However, when an action is dismissed for forum non conveniens, it must begin again as a new case in a new court, and that court will, of course, not be bound to apply the law the court that dismissed the action would have applied. It can be argued, then, that a forum non conveniens dismissal has such significant substantive consequences that it must be treated as a matter of substantive law.

A transfer within the federal system under 28 U.S.C. section 1406, which permits transfer of an action from a court where venue is improper to a court where the action could properly have been brought, will also result in a change in the governing law. 28 U.S.C. § 1406 (1988). Under section 1406, the transferee court applies its own law to the action. *Nelson v. International Paint Co.*, 716 F.2d 640, 643 (9th Cir. 1983). A section 1406 transfer must be considered procedural in the wake of *Ricoh*, and therefore the fact that a forum non conveniens dismissal will result in a change of law is not

If the courts were to conclude that forum non conveniens is a matter of substantive law, this would not necessarily preclude the application of federal law to such determinations in FSIA cases.<sup>95</sup> The FSIA does not establish new rules of liability but merely provides that a foreign state be liable to the same extent as would a private party in like circumstances.<sup>96</sup> Thus, in some instances, the rules of decision in an FSIA case will be those of state law.<sup>97</sup> However, the Supreme Court has noted that the FSIA is to some extent substantive in nature.<sup>98</sup> Since one of the primary objectives of the FSIA is to promote uniformity in the treatment of actions involving foreign sovereigns,<sup>99</sup> it seems likely that even if forum non conveniens is eventually held to be a matter of substantive law requiring the application of state rules in diversity actions, the federal courts would continue to make these determinations under federal law in FSIA actions.<sup>100</sup>

If federal law is applied to forum non conveniens determinations in FSIA actions, either because forum non conveniens is considered procedural or because federal substantive law is held to govern such questions under the FSIA, the courts will likely apply the rule of *Bremen* to a defendant's motion to dismiss a case brought in the contractual forum on the ground of forum non conveniens, just as they do in passing on a defendant's motion to dismiss a case brought outside of that forum.<sup>101</sup> The rule of *Bremen* is, in essence, a stricter form of

determinative of the substance/procedure question.

In the absence of decisive precedent, the question of whether forum non conveniens is a doctrine of substantive or of procedural law must be regarded as still open.

<sup>95</sup> See *supra* notes 59-67 and accompanying text.

<sup>96</sup> 28 U.S.C. section 1606 provides in pertinent part: "As to any claim for relief with respect to which a foreign state is not entitled to immunity . . . , the foreign state shall be liable in the same manner and to the same extent as a private individual under like circumstances. . . ." 28 U.S.C. § 1606 (1988).

<sup>97</sup> For a discussion of the controversy surrounding the application of state substantive law under the FSIA, see Crockett, *The Liability of Foreign States: The Role of Foreign Municipal Law*, 11 N.C.J. INT'L L. & COM. REG. 51, 62-64 n.51 (1986).

<sup>98</sup> *Verlinden v. Central Bank of Nigeria*, 461 U.S. 480, 496-97 (1983).

<sup>99</sup> *First Nat'l City Bank v. Banco Para el Comercio Exterior de Cuba*, 462 U.S. 611, 622 n.11 (1983); *Verlinden*, 461 U.S. at 489. See H.R. REP. NO. 1487, 94th Cong., 2d Sess. 32, reprinted in 1976 U.S. CODE CONG. & ADMIN. NEWS 6604, 6631.

<sup>100</sup> Most federal courts have thus far applied federal law to the issue in FSIA cases without any discussion of the issue. See *L'Europeene de Banque v. La Republica de Venezuela*, 700 F. Supp. 114, 119-20 (S.D.N.Y. 1988); *Hatzlachh Supply, Inc. v. Savannah Bank of Nigeria*, 649 F. Supp. 688, 692-93 (S.D.N.Y. 1986); *Crimson Semiconductor, Inc. v. Electronum*, 629 F. Supp. 903, 908-10 (S.D.N.Y. 1986); *Castillo v. Shipping Corp. of India*, 606 F. Supp. 497, 503-04 (S.D.N.Y. 1985). But see *Barkanic v. Gen. Admin. of Civil Aviation of the People's Republic of China*, No. 90-7641 (2d Cir. Jan. 14, 1991) (LEXIS, Genfed library) (the FSIA mandates the application of the forum state's choice of law rules, rather than federal choice of law rules).

<sup>101</sup> The federal courts have not indicated that the *Bremen* standard applies only when a plaintiff brings suit outside the contractual forum and have applied that stan-

forum non conveniens analysis since it displaces "normal forum non conveniens doctrine applicable in the absence of [a forum selection] clause."<sup>102</sup> The language of *Bremen* does not distinguish between plaintiffs' and defendants' attempts to resist the contractual forum,<sup>103</sup> and announces a strong preference for upholding a forum selection clause whenever it is fair to do so: "There are compelling reasons why a freely negotiated private international agreement, unaffected by fraud, undue influence, or overweening bargaining power . . . should be given full effect."<sup>104</sup> There is no obvious reason why this two-level test

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dard without comment to a defendant's motion to dismiss a case brought in the contractual forum. *L'Europeene de Banque*, 700 F. Supp. at 123; *First Interstate Leasing Serv. v. Sagge*, 697 F. Supp. 744, 746 (S.D.N.Y. 1988).

<sup>102</sup> 407 U.S. 1, 6 (1972).

<sup>103</sup> In fact, in *Bremen*, although the action was commenced outside the contractual forum, the motion was styled, in part, as a motion to dismiss for forum non conveniens, and the Court referred alternatively to specific enforcement of the forum selection clause, 407 U.S. at 15, and to the doctrine of forum non conveniens. *Id.* at 19.

Gruson has suggested that federal courts hold plaintiffs beginning actions outside the contractual forum to the harsh *Bremen* standard when ruling on motions for transfer of the action back to the contractual forum or for dismissal where such transfer is not available. In contrast, these courts determine motions by defendants for transfer from the contractual forum by the more relaxed standards of traditional forum non conveniens. See Gruson, *Controlling Site of Litigation*, *supra* note 11, at 36-39. Gruson's analysis does not, however, distinguish between motions for transfer pursuant to section 1404(a) and motions for dismissal for forum non conveniens. In each of the cases he cites to show a court applying a more lenient standard to a defendant, the motion under consideration was for transfer under section 1404(a). These cases are thus of limited use in predicting a court's approach to a defendant's motion to dismiss a case brought in the contractual forum on the ground of forum non conveniens.

The Supreme Court's recent decision in *Ricoh*, 487 U.S. 22 (1988), lends implicit support to the proposition that the standards for determination of a forum non conveniens motion should not vary according to the procedural posture of the case. In *Ricoh*, the Court held that the effect of a forum selection clause on a motion to transfer pursuant to section 1404(a) must always be evaluated under that statute's criteria, and those criteria do not vary with the procedural posture of the case. 487 U.S. at 32. If courts apply the same standard to a motion to transfer an action brought outside the contractual forum into that forum, and a motion to transfer a case brought in the contractual forum to another location, it would be inconsistent to draw a distinction between the standard of review applied in these two situations on a motion to dismiss for forum non conveniens and a motion to dismiss as a matter of substantive contract law.

See also *Credit Francais Int'l v. Sociedad Financiera de Comercio, C.A.*, 128 Misc.2d 564, 568, 490 N.Y.S.2d 670, 674-76 (Sup. Ct. 1985), which suggests that at least some New York state courts will apply the *Bremen* test to both a plaintiff's and defendant's attempts to evade a contractual forum.

<sup>104</sup> 407 U.S. at 12-13 (footnote omitted). It should be noted, however, that despite the policy favoring forum selection clauses, in some procedural settings there will be no right to immediate appeal from a judicial order refusing enforcement of a forum clause. The United States Supreme Court recently held that denial of a motion to dismiss based on enforcement of a forum clause selecting an alternate exclusive forum does not give rise to an immediate right of appeal. That is, it does not satisfy the requirements of the collateral order exception to the general rule that no appeal may be taken from an interlocutory order. *Lauro Lines s.r.l. v. Chasser*, 490 U.S. 495 (1989). The Court rested its holding on the proposition that the right sought to be protected by an immedi-

— examination of forum non conveniens motions under traditional factors when the case is not based on a contract containing a forum selection clause, and examination of such motions under the strict *Bremen* factors when it is — should not be used in FSIA cases.

Finally, when a plaintiff brings an action in the courts of a state other than New York, that state court judge would look to that state's rules to determine whether to dismiss an action brought in violation of an exclusive forum clause. Some states do not enforce forum selection clauses.<sup>105</sup> However, if suit is brought in those states, a sovereign defendant may remove the action to the federal court sitting in that locale and move in the federal court for dismissal on the ground of forum non conveniens or for a transfer under section 1404(a). As discussed above, a federal court in such a case would likely apply federal law to the motion to dismiss or transfer, regardless of the law of the state where the action was commenced, and would most likely enforce the forum selection clause.<sup>106</sup>

## 2.2. Choice of Law Clauses

A court faced with an agreement containing a governing law clause must determine both the enforceability and the scope of that clause. That is, the court must decide whether the clause calls for the application of the whole law of the chosen jurisdiction, including its

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ate appeal could be adequately vindicated by appeal following final judgment. For similar reasons, denial of a motion to dismiss for forum non conveniens cannot be appealed as of right. *Van Cauwenberghe v. Biand*, 486 U.S. 517, 527-29 (1988). In contrast, an order dismissing an action, whether for forum non conveniens, to specifically enforce a forum selection clause, or for any other reason, is immediately appealable. It is a final order that puts an end to litigation. See *Elfenbein v. Gulf & Western Indus.*, 590 F.2d 445, 447-49 (2d Cir. 1978); *United States v. Fluor Corp.*, 436 F.2d 383, 384-85 (2d Cir. 1970), *cert. denied*, 402 U.S. 945 (1971); *In re Lidoriki Maritime Corp.*, 410 F. Supp. 919, 921 (E.D. Pa. 1976), *aff'd mem. sub nom.* *Alexopolos v. Lidoriki Maritime Corp.*, 547 F.2d 1158 (3d Cir. 1977), *aff'd mem. sub nom.* *Brian v. Lidoriki Maritime Corp.*, 547 F.2d 1159 (3d Cir. 1977), *aff'd mem. sub nom.* *Kutlu v. Lidoriki Maritime Corp.*, 547 F.2d 1161 (3d Cir. 1977), *aff'd mem. sub nom.* *In re Lidoriki Maritime Corp.*, 547 F.2d 1162 (3d Cir. 1977), *aff'd mem. sub nom.* *Pimental v. Lidoriki Maritime Corp.*, 547 F.2d 1163 (3d Cir. 1977), *aff'd mem. sub nom.* *Tastekin v. Lidoriki Maritime Corp.*, 547 F.2d 1164 (3d Cir. 1977); 9 MOORE'S FEDERAL PRACTICE, *supra* note 86, at ¶¶ 110.13[1], 110.13[6].

An order granting or denying transfer under 28 U.S.C. § 1404(a), however, does not end the litigation and is therefore not immediately appealable as of right. *McCreary Tire & Rubber Co. v. CEAT S.p.A.*, 501 F.2d 1032, 1034 (3d Cir. 1974). Thus, the availability of interlocutory review of a judicial order granting or denying enforcement of a forum clause may depend in part on the procedural devices available to enforce the clause.

<sup>105</sup> See, e.g., *Ricoh*, 487 U.S. at 30 (Alabama law, if applicable, would not enforce forum selection clauses providing for out-of-state venues).

<sup>106</sup> See *supra* notes 80-100 and accompanying text.

choice of law rules, or only for its substantive law. New York state and federal courts are in agreement that a contractual choice of law clause will generally be enforced.<sup>107</sup>

### 2.2.1. New York Common Law Choice of Law Rules

New York state courts traditionally determine the enforceability of choice of law clauses under one of three competing conflicts of laws rules. Under the "reasonable relationship" test, the parties' choice of law will be upheld as long as the transaction bears a reasonable relationship to the jurisdiction whose law is selected.<sup>108</sup> Unfortunately there is no clear test for what constitutes a reasonable relationship to the jurisdiction.<sup>109</sup> Moreover, it is not clear to what extent the parties may validate a choice of law by structuring their transaction to provide contacts with their chosen jurisdiction.<sup>110</sup> Thus, this test leads to an undesirable lack of certainty. Furthermore, when faced with a governing law clause, New York state courts generally apply the reasonable relationship approach,<sup>111</sup> but in rare instances, a court may follow the "grouping of contacts" analysis. Under this approach, the substantive law of the jurisdiction having the most substantial contacts with a transaction will be held to govern the transaction and the parties' choice of law will be considered as merely an important contact to be considered by the court in the balancing process.<sup>112</sup>

Similarly, and again in rare instances, a court might follow the "governmental interest" test, under which the court examines the governmental purpose behind each of the conflicting rules of law and applies the substantive law of the jurisdiction having the greatest interest

<sup>107</sup> See, e.g., *Siegelman v. Cunard White Star Ltd.*, 221 F.2d 189, 193-95 (2d Cir. 1955); *Avant Petroleum, Inc. v. Banque Paribas*, 652 F. Supp. 542, 546 n.6 (S.D.N.Y. 1987), *aff'd*, 853 F.2d 140 (2d Cir. 1988); *Reger v. National Ass'n of Bedding Mfrs. Group Ins. Trust Fund*, 83 Misc. 2d 527, 543, 372 N.Y.S.2d 97, 117 (Sup. Ct. 1975) (citing supporting cases).

<sup>108</sup> See *Reger*, 83 Misc. 2d at 538-44, 372 N.Y.S.2d at 112-18. See also *Woodling v. Garrett Corp.*, 813 F.2d 543, 551 (2d Cir. 1987).

<sup>109</sup> See Gruson, *Controlling Choice of Law*, in SOVEREIGN LENDING: MANAGING LEGAL RISK 51, 57 (M. Gruson & R. Reisner eds. 1984) [hereinafter Gruson, *Controlling Choice of Law*].

<sup>110</sup> *Id.* See also *Seeman v. Philadelphia Warehouse Co.*, 274 U.S. 403, 408 (1927).

<sup>111</sup> See, e.g., *A.S. Rampell, Inc. v. Hyster Co.*, 3 N.Y.2d 369, 381-82, 144 N.E.2d 371, 379, 165 N.Y.S.2d 475, 486 (1957); *Gambar Enters. Inc. v. Kelly Servs., Inc.*, 69 A.D.2d 297, 303, 418 N.Y.S.2d 818, 822 (1979); *Reger*, 83 Misc. 2d at 539-41, 372 N.Y.S.2d at 114.

<sup>112</sup> *Haag v. Barnes*, 9 N.Y.2d 554, 559-60, 175 N.E.2d 441, 443-44, 216 N.Y.S.2d 65, 68-69 (1961). See *Triad Fin. Estab. v. Tumpane Co.*, 611 F. Supp. 157, 162-63 (N.D.N.Y. 1985). See also Gruson, *Contractual Choice of Law and Choice of Forum*, *supra* note 22, at 3 n.16, for a comprehensive list of cases so holding.

in the application of its law to the particular facts of the case. Under this test, no weight is given to the parties' own choice of law.<sup>113</sup> Under these circumstances, it is impossible for parties to be certain of the standard that will be used to judge the enforceability of a choice of law clause, and thus impossible to be certain, particularly in complex cases, that the clause will be effective.

### 2.2.2. *Choice of Law Rules under G.O.L. Section 5-1401*

G.O.L. section 5-1401<sup>114</sup> now permits parties to an agreement relating to a transaction involving not less than two hundred and fifty thousand dollars to make an enforceable election to have their agreement governed by New York law "whether or not such contract, agreement, or undertaking bears a reasonable relationship to this state."<sup>115</sup> This special provision relates only to cases where New York law is chosen. Thus, if the parties choose another governing law and litigate their disputes in the New York state courts, New York courts will presumably determine the enforceability of that clause under New York's traditional conflicts principles described above.

The language of section 5-1401 implies that the reasonable relationship test, rather than the governmental interest or the significant contacts tests, is the governing standard for the validity of a choice of law clause in New York. Thus, the statute overrides the reasonable relationship requirement for agreements that choose New York law and meet its minimum-value requirement. But, as some cases have suggested, a choice of law clause that meets the reasonable relationship test may nevertheless be overridden out of deference to policies of either the forum or another jurisdiction.<sup>116</sup> Nothing in section 5-1401 necessarily prohibits such action by a court. Rather, although no court has yet done so, section 5-1401 could be read to reflect a strong New York policy to be weighed in the balance, but not an absolute requirement that a court uphold a contractual choice of New York law in all situations where the statutory standard is met.<sup>117</sup> Thus, it remains theoreti-

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<sup>113</sup> See *Triad Fin. Estab.*, 611 F. Supp. at 162; *J. Zeevi & Sons, Ltd. v. Grindlays Bank (Uganda), Ltd.*, 37 N.Y.2d 220, 226-27, 333 N.E.2d 168, 172, 371 N.Y.S.2d 892, 898-99, *cert. denied*, 423 U.S. 866 (1975); *Intercontinental Planning, Ltd. v. Daystrom, Inc.*, 24 N.Y.2d 372, 382, 248 N.E.2d 576, 580-82, 300 N.Y.S.2d 817, 824-25 (1969).

<sup>114</sup> N.Y. GEN. OBLIG. LAW § 5-1401 (McKinney 1989). For the text of this statute, see *supra* note 25.

<sup>115</sup> *Id.*

<sup>116</sup> *Siegelman v. Cunard White Star, Ltd.*, 221 F.2d 189, 195 (2d Cir. 1955).

<sup>117</sup> In this regard, section 5-1401 differs significantly from section 5-1402, with its corresponding C.P.L.R. 327(b) enforcement mechanism. N.Y. CIV. PRAC. L. & R. 327(b) (McKinney 1990). See *supra* note 51. One result of such a holding could be

cally possible that even under the new statute, a court following New York choice of law rules might refuse to enforce a choice of New York law for policy reasons.<sup>118</sup>

### 2.2.3. *State v. Federal Choice of Law Rules*

There is some controversy over whether federal courts should determine the enforceability of a choice of law clause under state or federal conflicts rules when jurisdiction is premised on the FSIA.<sup>119</sup> The language of the FSIA provides no clear answer to the question, and the courts have yet to conclusively resolve it. In *First National City Bank v. Banco Para el Comercio Exterior de Cuba*,<sup>120</sup> the Supreme Court stated in dictum that the FSIA did not require the application of state conflicts rules, even though the FSIA might mandate the application of state rules of liability in some circumstances.<sup>121</sup> In that case, the Court applied federal choice of law principles.<sup>122</sup> Lower federal courts have applied both federal and state choice of law rules in federal question cases. In *Corporacion Venezolana de Fomento v. Vintero Sales Corp.*,<sup>123</sup> for example, the court applied federal choice of law principles<sup>124</sup> in a contract action. In that case, the court's jurisdiction was

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that, in a case where the parties had chosen New York State law pursuant to section 5-1401, and the requirements of section 5-1402 were met but public policy prevented the application of New York State law, the New York state courts would nevertheless be precluded from dismissing the case for forum non conveniens under C.P.L.R. 327(b). Under such circumstances, the court would retain the case but apply whatever law was applicable under standard choice of law rules.

<sup>118</sup> See *Triad Fin. Estab. v. Tumpane Co.*, 611 F. Supp. 157, 162-66 (N.D.N.Y. 1985) (under pre-1984 law, the court refused to enforce a sales agency contract that was valid under New York law and which contained a choice of law clause calling for application of New York law. This refusal occurred because the contract violated a Saudi Arabian decree which prohibited the payment of any agent's commission in connection with the sale of arms, and Saudi Arabia had a materially greater interest in the controversy).

<sup>119</sup> See Gruson, *Controlling Choice of Law*, *supra* note 109, at 52-53.

<sup>120</sup> 462 U.S. 611 (1983).

<sup>121</sup> *Id.* at 622 n.11.

<sup>122</sup> *Id.* at 621-23.

<sup>123</sup> 629 F.2d 786 (2d Cir. 1980), *cert. denied*, 449 U.S. 1080 (1981).

<sup>124</sup> Gruson has suggested that the court in *Venezolana* applied New York choice of law principles to validate the parties' choice of law as applied to one set of issues in this case. See Gruson, *Controlling Choice of Law*, *supra* note 109, at 53. The *Venezolana* court's language on the point is not clear, but it seems more probable that it applied federal choice of law rules. The court stated explicitly that, as this was not a diversity case, it was not bound to follow state choice of law rules, and explicitly followed federal rules to choose a governing law as to a second set of issues in the case. *Venezolana*, 629 F.2d at 795. As to the first set of issues, the court stated: "Since there are enough contacts with New York to validate the parties' choice of New York law as governing under any choice of law analysis, we need not reach the question of what jurisdiction's law would be applied if a serious challenge to the parties' ability to choose

founded on the Edge Act,<sup>125</sup> which, like the FSIA, grants the courts federal question jurisdiction.<sup>126</sup> However, in *Barkanic*,<sup>127</sup> the court applied state choice of law rules in a FSIA action. At least one federal court outside of New York has followed *Venezolana* and applied federal choice of law rules in FSIA actions.<sup>128</sup>

Federal choice of law rules, which are very similar to New York's traditional conflicts of law rules, generally give effect to a governing law provision. In the seminal case of *Siegelman v. Cunard White Star, Ltd.*,<sup>129</sup> the court noted that federal conflicts law will give effect to the parties' intent with respect to governing law as long as the law chosen is that of a jurisdiction that bears a reasonable relationship to the transaction and its application does not contravene an important policy of an interested state.<sup>130</sup> Federal courts, therefore, will still look for some relationship with the chosen state. Hence, they will not always enforce a choice of New York law that would be binding upon the New York state courts under section 5-1401.

In any case where the parties to an agreement have made a valid choice of governing law, the court must determine whether their choice refers to the whole law of the chosen jurisdiction, including its choice of

New York law could be mounted." *Id.* at 794-95. In light of the court's comments about the applicability of federal choice of law rules, it seems more reasonable to read this language to mean that it found it unnecessary to decide what the federal standard for evaluating a choice of law clause should be, not that it was unnecessary to choose between state and federal choice of law rules.

<sup>125</sup> 12 U.S.C. § 632 (1989). The Edge Act grants federal jurisdiction over "all suits of a civil nature . . . to which any corporation organized under the laws of the United States shall be a party, arising out of transactions involving international or foreign banking. . . ." *Id.*

<sup>126</sup> *Venezolana*, 629 F.2d at 795.

<sup>127</sup> *Barkanic v. Gen. Admin. of Civil Aviation of the People's Republic of China*, No. 90-7641 (2d Cir. Jan. 14, 1991) (LEXIS, Genfed library).

<sup>128</sup> *Harris v. Polskie Linie Lotnicze*, 820 F.2d 1000, 1003 (9th Cir. 1987).

<sup>129</sup> 221 F.2d 189 (2d Cir. 1955).

<sup>130</sup> *Id.* at 195. See also RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 187 (1971) (cited in *Harris*, 820 F.2d at 1003, as a source of federal choice-of-law principles). The *Restatement* provides, in pertinent part:

(2) The law of the state chosen by the parties to govern their contractual rights and duties will be applied, even if the particular issue is one which the parties could not have resolved by an explicit provision in their agreement directed to that issue, unless either

(a) the chosen state has no substantial relationship to the parties or the transaction and there is no other reasonable basis for the parties' choice, or

(b) application of the law of the chosen state would be contrary to a fundamental policy of a state which has a materially greater interest than the chosen state in the determination of the particular issue and which, under the rule of § 188, would be the state of the applicable law in the absence of an effective choice of law by the parties.

law rules, or whether it refers to the substantive law only.<sup>131</sup> Although there is no decisive New York precedent on the question,<sup>132</sup> common sense and what authority there is on the point both suggest that such a clause should be held to refer only to the substantive law of the chosen jurisdiction. As this Article surely illustrates, specification of any jurisdiction's choice of law rules will not necessarily give the parties the advantages of predictability and clarity that are the major reasons for making a contractual choice of law. Recognizing this, the court in *Siegelman*<sup>133</sup> held that the contractual choice of English law referred to the substantive law of England, "for surely the major purpose of including the provision in the ticket was to assure Cunard of a uniform result in any litigation no matter . . . where the litigation arose, and this result might not obtain if the 'whole' law of England were referred to."<sup>134</sup> Moreover, the *Restatement (Second) of Conflict of Laws*, which has been cited with approval in both New York state and federal cases,<sup>135</sup> suggests that only the substantive law of the chosen jurisdiction should be applied.<sup>136</sup> It therefore seems likely that either a federal court

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<sup>131</sup> This is the question of the applicability of the conflicts-of-laws doctrine known as *renvoi*. The court explained, in *Reger v. National Ass'n of Bedding Mfrs. Group Ins. Trust Fund*, 83 Misc. 2d 527, 543, 372 N.Y.S.2d 97, 117 (Sup. Ct. 1975), that "[t]he process of referring back to the foreign jurisdiction's conflict of laws rules is known as *renvoi*—the doctrine of remission, whereby the forum State looks to the whole law of the foreign jurisdiction. . . ." The difficulties caused by the application of *renvoi* may be easily illustrated. If two California citizens make a contract which contains a provision selecting New York law and which does not satisfy the requirements of G.O.L. section 5-1401, and suit is later brought on the agreement in a California court, that court, assuming it recognizes the governing law provision as valid, will have to decide whether to apply *renvoi*. If it were to do so, it might well conclude that a New York court, applying New York's reasonable relationship test to the governing law provision, would invalidate the governing law clause and apply California's substantive law to the action. The California court, then, would by application of New York's whole law, decide the dispute under California's substantive law—hardly the result the parties are likely to have anticipated when they stipulated the law of New York.

<sup>132</sup> See Gruson, *Controlling Choice of Law*, *supra* note 109, at 62.

<sup>133</sup> 221 F.2d 189 (2d Cir. 1955).

<sup>134</sup> *Id.* at 194.

<sup>135</sup> *Harris v. Polskie Linie Lotnicze*, 820 F.2d 1000, 1003 (9th Cir. 1987); *Reger*, 83 Misc. 2d at 539, 372 N.Y.S.2d at 113.

<sup>136</sup> The RESTATEMENT (SECOND) OF CONFLICT OF LAWS provides:

(1) The law of the state chosen by the parties to govern their contractual rights and duties will be applied. . . .

(3) In the absence of a contrary indication of intention, the reference is to the local law of the state of the chosen law.

Comment h elaborates:

The reference, in the absence of a contrary indication of intention, is to the "local law" of the chosen state and not to that state's "law," which means the totality of its law including its choice-of-law rules. When they choose the state which is to furnish the law governing the validity of their

or a New York court would apply only the substantive law of a chosen jurisdiction when presented with a valid choice of law clause.

### 3. DOES THE FOREIGN SOVEREIGN IMMUNITIES ACT OF 1976 PROVIDE A DEFENSE TO A SOVEREIGN DEBTOR IN AN ACTION COMMENCED IN THE UNITED STATES?

#### 3.1. *Jurisdiction over a Foreign State Under the FSIA*

The FSIA provides that "a foreign state shall be immune from the jurisdiction of the courts of the United States and of the States except as provided in sections 1605 and 1607 of this chapter."<sup>137</sup> Those sections specifically authorize a foreign state to waive such immunity "either explicitly or by implication."<sup>138</sup> Sovereign debt agreements virtually always contain an express provision which conditions the extension of credit upon the borrower's waiving its sovereign immunity to the full extent permitted under the FSIA. Thus, the immunity from jurisdiction granted to sovereigns by the FSIA does not provide a sovereign debtor with a defense to an action commenced in any court in the United States for repayment of a debt due under such an agreement.<sup>139</sup> Accordingly, a court typically will be able to adjudicate claims against a sovereign debtor to the same extent it can adjudicate claims against any other defendant, subject to the procedural rules discussed in section 1.<sup>140</sup> Only in those rare instances where an enforceable waiver of sovereign immunity is not contained in a sovereign debt agreement will a court be required to go through the analysis of whether the sovereign has lost its immunity by reason of the application of any of the debated provisions of sections 1605 and 1607 of the FSIA.<sup>141</sup>

#### 3.2. *Attachment and Execution Under the FSIA: An Overview*

To enforce a judgment entered against a sovereign debtor in the

contract, the parties almost certainly have the "local law," rather than the "law," of that state in mind. To apply the "law" of the chosen state would introduce the uncertainties of choice of law into the proceedings and would serve to defeat the basic objectives, namely those of certainty and predictability, which the choice-of-law provision was designed to achieve.

RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 187 comment h (1971) (citations omitted).

<sup>137</sup> 28 U.S.C. § 1604 (Supp. 1990).

<sup>138</sup> 28 U.S.C. § 1605(a)(1)(Supp. 1990).

<sup>139</sup> Moreover, such waiver of jurisdictional immunity is also likely to be an effective waiver of any immunity the sovereign may have in any other foreign jurisdiction where an action could be commenced.

<sup>140</sup> See *supra* notes 3-10 and accompanying text.

<sup>141</sup> 28 U.S.C. §§ 1605, 1607 (Supp. 1990).

event it is not voluntarily paid, or to ensure that any eventual judgment will be satisfied, a creditor may seek to effectuate either prejudgment attachment or post-judgment attachment (or execution) of assets of the debtor located in the United States or elsewhere. Although, as discussed above, sovereign immunity typically will not provide an effective defense to the entry of an adverse judgment against a sovereign debtor, it may effectively prevent enforcement of such a judgment. It should be noted, however, that even if the judgment is not enforceable against the defendant's assets, it may have onerous negative repercussions for the sovereign debtor. For example, the judgment may constitute a cross-default under the debtor's various loan agreements.

The FSIA provides that "the property in the United States of a foreign state shall be immune from attachment[,] arrest and execution,"<sup>142</sup> subject to the exceptions set forth in the FSIA and to "existing international agreements" to which the United States was a party at the time of enactment of the FSIA in 1976.<sup>143</sup> Section 1610(a) of the FSIA creates an exception to this general rule, and provides that property of a government or any subdivision, agency or instrumentality that is "used for a commercial activity in the United States" *and* as to which there has been a waiver of immunity, is not immune from execution after judgment.<sup>144</sup> In addition, section 1610(b) of the FSIA provides that property of a governmental agency or instrumentality other than the government itself (and other than a central bank acting for its own account, to which special rules apply) which is "engaged in commercial activity in the United States" is not immune from execution after judgment *either* (a) where the agency or instrumentality has waived immunity, *or* (b) where the judgment relates to a claim based on the agency's or instrumentality's commercial activity in the United States.<sup>145</sup> Finally, section 1611(b)(1) of the FSIA provides a specific immunity from post-judgment attachment for property of a central bank or monetary authority "held for its own account" unless there has been an "explicit" waiver of immunity by the central bank or parent government.<sup>146</sup> This latter provision is particularly relevant since it is often a foreign state's "central bank or monetary authority" which is designated either as a borrower or as a guarantor under the foreign state's loan agreements, and whose assets, therefore, may be looked to in order to satisfy any judgment rendered thereunder.

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<sup>142</sup> *Id.* § 1609.

<sup>143</sup> *Id.* § 1604.

<sup>144</sup> *Id.* § 1610(a).

<sup>145</sup> *Id.* § 1610(b).

<sup>146</sup> *Id.* § 1611(b)(1). See *infra* note 178 and accompanying text.

In addition to these general rules regarding post-judgment attachment and execution, section 1610(d) of the FSIA provides for *prejudgment* attachment of commercial property of a foreign state located in the United States where there has been an "explicit" waiver of immunity to prejudgment attachment (i.e., a waiver that refers specifically to prejudgment attachment).<sup>147</sup> This provision probably does not apply to the property of a foreign central bank held for its own account, as it is likely to be considered absolutely immune from prejudgment attachment, though not from post-judgment attachment or execution, even if the central bank purports explicitly to have waived such immunity.

### 3.3. *Prejudgment Attachment*

#### 3.3.1. *Prejudgment Attachment Generally*

Prejudgment attachment is a procedure by which, prior to adjudication on the merits of a case, a court may order the seizure of a portion of the defendant's assets to secure satisfaction of a judgment that may ultimately be given. The standards governing the granting of an order of prejudgment attachment, as well as other provisional remedies in either federal or state court, are governed by state law<sup>148</sup> and will therefore vary by jurisdiction.<sup>149</sup>

Notwithstanding such state rules allowing prejudgment attachment, the FSIA grants foreign sovereign debtors certain immunities

<sup>147</sup> *S & S Mach. Co. v. Masinexportimport*, 706 F.2d 411, 413-18 (2d Cir. 1983), *cert. denied*, 464 U.S. 850 (1983).

<sup>148</sup> FED R. CIV. P. 64.

<sup>149</sup> For example, in an action pending in a state or federal court in New York State:

An order of attachment may be granted in any action . . . where the plaintiff has demanded and would be entitled, in whole or in part, or in the alternative, to a money judgment against one or more defendants, when:

1. the defendant is a nondomiciliary residing without the state, or is a foreign corporation not qualified to do business in the state; or
2. the defendant resides or is domiciled in the state and cannot be personally served despite diligent efforts to do so; or
3. the defendant, with intent to defraud his creditors or frustrate the enforcement of a judgment that might be rendered in plaintiff's favor, has assigned, disposed of, encumbered or secreted property, or removed it from the state or is about to do any of these acts; or
4. the cause of action is based on a judgment, decree or order of a court of the United States or of any other court which is entitled to full faith and credit in this state, or on a judgment which qualifies for recognition under the provisions of article 53.

N.Y. CIV. PRAC. L. & R. § 6201 (McKinney 1980). Since a sovereign debtor is considered a non-domiciliary residing outside the state of New York, absent immunity, its assets located in New York would normally be subject to prejudgment attachment.

from prejudgment attachment. Section 1610(d) of the FSIA provides that property "used for a *commercial activity* in the United States" (other than central bank property held for the central bank's own account, which is governed by a special rule) is not immune from prejudgment attachment if such immunity has been "explicitly waived."<sup>150</sup> In their loan agreements, in addition to waiving any sovereign immunity as to jurisdiction, foreign sovereign debtors typically explicitly waive any immunity from prejudgment attachment within the meaning of this provision. This waiver would therefore render all of the sovereign debtor's commercial assets<sup>151</sup> subject to prejudgment attachment, and would also subject to prejudgment attachment any commercial assets of a central bank *not* "held for its own account." In this regard, the FSIA expressly provides that the following assets are *not* subject to prejudgment attachment (nor to post-judgment attachment or execution) under any circumstances: (1) property of certain designated organizations such as the International Monetary Fund or the World Bank to the extent that attachment would "imped[e] the disbursement of funds to, or on the order of, a foreign state," and (2) certain property used or intended to be used in connection with military activity.<sup>152</sup>

In addition to the legal rules governing prejudgment attachment of a sovereign debtor's assets, a number of practical considerations regarding prejudgment attachment merit discussion. In state and federal courts in New York and in the United States generally, when an action is commenced, an order of prejudgment attachment may be obtained against assets located in the jurisdiction *without prior notice* to the party whose assets are seized.<sup>153</sup> Thus, if a court sitting in New York were to grant an *ex parte* order of prejudgment attachment against a sovereign debtor's assets, which would include all of its bank accounts

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<sup>150</sup> 28 U.S.C. § 1610(d) (Supp. 1990) (emphasis added).

<sup>151</sup> The "commercial" status of a given asset will be evaluated by the "nature" of the activity for which it is being used, rather than by the purpose of the activity from the viewpoint of the foreign government. 28 U.S.C. § 1603(d) (Supp. 1990). See H.R. REP. NO. 1487, 94th Cong., 2d Sess., reprinted in 1976 U.S. CODE CONG. & ADMIN. NEWS 6604, 6615. This standard is often difficult to apply in practice. In one case, for instance, execution was permitted on a foreign embassy's bank account because it was used in part to pay for various "commercial" goods and services such as the hiring of American clerical staff. See *Birch Shipping Corp. v. Embassy of the United Republic of Tanzania*, 507 F. Supp. 311 (D.D.C. 1980). The better view, however, is that embassy bank accounts should be immune from execution even if they are used partly for commercial activities in connection with running the embassy. *Liberian E. Timber Corp. v. Government of the Republic of Liberia*, 659 F. Supp. 606 (D.D.C. 1987) (dicta).

<sup>152</sup> 28 U.S.C. §§ 1611(a), 1611(b)(2)(1988); International Organizations Immunities Act, 22 U.S.C. § 288 (1988).

<sup>153</sup> Conversely, if a lender were to commence an action against a defendant in a jurisdiction other than New York, it could not obtain prejudgment attachment of assets of the defendant located in New York.

in the State of New York, the order could be served on all commercial banks in New York, as well as on the Federal Reserve Bank of New York ("FRBNY"), and on any other potential garnishee in New York (i.e., an investment bank), before the sovereign borrower was advised that the order had been granted. Upon receipt of the order, a commercial bank, the FRBNY, investment bank, or other garnishee would be required to give custody to the sheriff of all of that defendant's accounts, including any monies transferred into such an account between the time of receipt of the order and the time that payment to the sheriff was actually made. In other words, until such time as the order of attachment were vacated, the defendant would not only lose control over the assets attached, but would also be greatly hampered, if not totally precluded, from conducting financial transactions with banks in New York.

In order to obtain an *ex parte* order of prejudgment attachment of assets of a sovereign or other debtor, a creditor would have to convince a court that it "would be entitled, in whole or in part, or in the alternative, to a money judgment against [the defendant]" and that "the defendant is a non-domiciliary residing without the state, or is a foreign corporation not authorized to do business in the state. . . ."<sup>154</sup> Formal notice to the party whose assets have been attached, and judicial consideration of whether the order of attachment should be confirmed or vacated (for reasons of sovereign immunity or otherwise), occurs *after* the prejudgment attachment has been made. It is therefore possible for a creditor to obtain a prejudgment attachment that is legally improper (because, for example, it attaches non-commercial property of the defendant, central bank assets "held for its own account," or property of some other state agency or instrumentality that is not a party to the agreements) and nevertheless be able to tie up the assets involved for a period of weeks or even months until a court rules on the propriety of the attachment.

A factor that militates against a plaintiff seeking an order of prejudgment attachment, at least in courts sitting in New York, is the rule that a creditor found to have wrongfully attached property is subject to absolute liability for all injuries flowing from the wrongful attachment.<sup>155</sup> This threat of liability for wrongful attachment, without regard to the reasonableness of the creditor's actions, would tend to deter unwarranted attachments. In particular, in light of the fairly clear prohibition against such attachments under the FSIA with respect to prop-

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<sup>154</sup> N.Y. CIV. PRAC. L. & R. 6201 (McKinney 1980).

<sup>155</sup> FED. R. CIV. P. 64; N.Y. CIV. PRAC. L. & R. 6212(e) (McKinney 1980).

erty held for the central bank's own account, the threat of liability for wrongful attachment would tend to discourage prejudgment attachment of central bank property.

### 3.3.2. *Immunity For Foreign Central Bank Assets "Held For Its Own Account"*

As noted above, the property of foreign central banks is subject to a special rule contained in section 1611(b)(1) of the FSIA:<sup>156</sup>

Notwithstanding the provisions of section 1610 of this chapter, the property of a foreign state shall be immune from attachment and from execution, if-

(1) the property is that of a foreign central bank or monetary authority held for its own account, unless such bank or authority, or its parent foreign government, has explicitly waived its immunity from attachment in aid of execution, or from execution, notwithstanding any withdrawal of the waiver which the bank, authority or government may purport to effect except in accordance with the terms of the waiver. . . .<sup>157</sup>

The special rule contained in section 1611(b)(1) for central bank property thus differs from the rule applicable to property of other foreign governmental entities in two important respects. First, the criterion for immunity under section 1611(b)(1) is whether the property is that (i) "of a foreign central bank" which is (ii) "held for its own account," rather than merely whether the property is "used for a commercial activity." Second, although the general rule of section 1610 permits a foreign state to waive prejudgment attachment as well as post-judgment

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<sup>156</sup> According to Ernest Patrikis (Executive Vice-President and General Counsel of the FRBNY, but not purporting to be enunciating FRBNY policy on this issue), the reasons for granting special treatment to the property of foreign central banks are: (1) foreign central banks typically invest a large portion of their reserves in foreign currency obligations, particularly United States dollar obligations, because of the large and relatively stable United States financial market; (2) the removal of large amounts of foreign central bank funds from the United States could have an "immediate and adverse effect on the U.S. balance of payments;" (3) "the removal of that portion of foreign central bank reserves invested in U.S. government securities could seriously affect that nation's ability to manage the public debt;" and (4) U.S. foreign relations could be adversely affected by prejudgment attachment of foreign central bank assets. Patrikis, *Immunity of Central Bank Assets Under US Law*, in SOVEREIGN LENDING: MANAGING LEGAL RISK 89 (M. Gruson & R. Reisner eds. 1984). See also H.R. REP. NO. 1487, 94th Cong., 2d Sess., reprinted in 1976 U.S. CODE CONG. & ADMIN. NEWS 6604, 6630.

<sup>157</sup> 28 U.S.C. § 1611(b) (1988) (emphasis added).

attachment, section 1611(b)(1) speaks only of the waiver by foreign central banks of *post-judgment* attachment. Accordingly, although commentators have questioned the intent of Congress, most agree that the language in section 1611(b)(1) means that foreign central banks *cannot* effectively waive immunity from prejudgment attachment for property held for their own account.<sup>158</sup>

Under these standards, the immunity of a central bank's assets from prejudgment attachment hinges upon whether such assets are held for the central bank's "own account." This concept is not defined in the FSIA and has not been the subject of any significant judicial interpretation.<sup>159</sup> The legislative history of the FSIA, however, suggests that it refers to property used by a foreign central bank to conduct its central bank activities. A letter from the United States Department of Justice and Department of State to the President of the United States Senate analyzing section 1611(b)(1) of the FSIA states in part that:

Section 1611(b)(1) applies to funds of a foreign central bank . . . which are deposited in the United States and "held" for the bank's . . . "own account"—i.e., funds used or held in connection with central banking activities, as distinguished from funds used solely to finance the commercial transactions of other entities or of foreign states.<sup>160</sup>

Central banking activities would clearly include the custody and management of a country's international monetary assets, including foreign exchange, gold, and foreign securities. If circumstances were to arise in which the ownership of assets held by a central bank in the United States might be subject to question (i.e., if a central bank were itself merely a custodian) or if a central bank held assets in the United States in connection with activities which might arguably be characterized as something other than ordinary central banking activities (i.e., if

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<sup>158</sup> *Banque Compafina v. Banco de Guatemala*, 583 F. Supp. 320, 322-23 (S.D.N.Y. 1984) (dictum); Nichols, *Sovereign Debtors Under US Immunity Law*, in *SOVEREIGN LENDING: MANAGING LEGAL RISK* 81, 85-86 (M. Gruson & R. Reisner eds. 1984); Patrikis, *supra* note 156, at 94; Brower, Bistline & Loomis, *The Foreign Sovereign Immunities Act of 1976 in Practice*, 73 AM. J. INT'L L. 200, 209 (1979). *But see* Nichols, *The Impact of the Foreign Sovereign Immunities Act on the Enforcement of Lenders' Remedies*, 1982 U. ILL. L. REV. 251, 260 (although the FSIA fails to validate a central bank's explicit waiver of its immunity from prejudgment attachment, "it is difficult to see why a court should decline to hold a central bank to its bargain on this point").

<sup>159</sup> One case notes in passing that letters of credit may not constitute assets of a central bank held for its own account, but does not discuss the issue in any meaningful way. *Werner Lehara Int'l, Inc. v. Harris Trust & Sav. Bank*, 484 F. Supp. 65, 75 (W.D. Mich. 1980).

<sup>160</sup> 1976 U.S. CODE CONG. & ADMIN. NEWS 6604, 6630.

a central bank were holding funds of other public sector or private entities in connection with issuing or confirming commercial letters of credit on their behalf), it would be necessary to examine closely the relevant facts and circumstances before a court could conclude that such assets were immune from attachment.

Were a court to hold that the special provisions of section 1611(b)(1) do not apply to a central bank's assets because, for example, the assets in question were not held in connection with normal central bank activities, then the general rules of section 1610(d) mentioned above would apply. Under these rules, a central bank's waiver of immunity from prejudgment attachment would be effective as to property "used for a commercial activity in the United States."<sup>161</sup>

It should be emphasized that even central bank assets held for "its own account" would still be subject to *post-judgment* attachment (or execution) to the extent that a central bank had explicitly waived its immunity from post-judgment attachment in accordance with section 1611(b) of the FSIA.

### 3.4. Remedies Similar to Prejudgment Attachment

Attachment is not the only remedy to which a resourceful creditor may resort in order to gain control over a debtor's property. Court-ordered provisional remedies such as preliminary injunctions or temporary restraining orders, as well as the self-help remedy of set-off frequently used by banks, have the same practical effect as prejudgment attachment. That is, debtors lose control of the funds affected by the remedy until there has been an adjudication of the merits of the controversy by a court. However, although the FSIA does not expressly limit the use of such remedies, commentators and courts have concluded that, at least in certain circumstances, the provisions and policies of the FSIA may limit the availability of such alternative remedies.

Injunctions and temporary restraining orders can only be imposed by court order. Hence, these remedies are similar in nature to prejudgment attachment. A court should recognize the policies behind the immunity from prejudgment attachment accorded foreign central banks by the FSIA and should *not* enjoin a central bank from removing assets from the court's jurisdiction that are immune from prejudgment attachment. On the other hand, courts can probably be expected to give effect to non-judicial remedies such as a bank's right of set-off without regard to the provisions of the FSIA.

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<sup>161</sup> 28 U.S.C. § 1610(d) (1988).

### 3.4.1. Preliminary Injunctions And Temporary Restraining Orders

An injunction is an equitable remedy whereby a court orders a party to do or not to do a specific act. For example, if a central bank debtor had funds on deposit with a New York bank, a creditor of the central bank might, under appropriate circumstances, seek to obtain an injunction from a court in New York forbidding the central bank from removing its funds from the New York bank. The practical effect of such an injunction, like that of prejudgment attachment, would be to ensure that assets of the central bank within the jurisdiction of the court at the outset of litigation would remain there and be available to satisfy any judgment that might ultimately be rendered against the central bank. An injunction can only be issued after a hearing which gives each party the opportunity to argue why the injunction should or should not be issued.

A temporary restraining order is similar to an injunction except that it is only granted for the limited period of time necessary to determine the appropriateness of granting an injunction. Under certain circumstances, a court may grant a temporary restraining order *without notice* to the defendant if the plaintiff can demonstrate that immediate and irreparable injury will result unless the defendant is restrained before a hearing can be held.<sup>162</sup> However, unlike prejudgment attachments, which are routinely granted *ex parte* in New York state courts (and to a lesser degree in New York federal courts), federal judges in New York will not grant *ex parte* temporary restraining orders except under the most extraordinary circumstances.

The question therefore arises whether the protections afforded a foreign sovereign debtor under the FSIA apply with the same force to a creditor seeking to enjoin a debtor from moving its assets outside the jurisdiction, as they do to a creditor seeking to attach those assets at the outset of litigation. The United States Court of Appeals for the Second Circuit held that a Romanian trading company that was protected from prejudgment attachment by the FSIA could likewise *not* be enjoined from drawing under certain irrevocable letters of credit opened in its favor. The court stated:

The FSIA would become meaningless if courts could eviscerate its protections merely by denominating their restraints as injunctions against the negotiation or use of property rather than as attachments of that property. We hold that courts in

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<sup>162</sup> FED. R. CIV. P. 65(b).

this context may not grant, by injunction, relief which they may not provide by attachment.<sup>163</sup>

Further discussion of the limitations the FSIA places on all court ordered provisional remedies is found in *S & S Mach. Co. v. Masinexportimport*<sup>164</sup> and *Raji v. Bank Sepah-Iran*.<sup>165</sup> Although these cases were decided under section 1610(d) of the FSIA (and *not* under section 1611(b), since a central bank was not involved), the conclusion of the two courts should also be applicable to the latter section based on the purposes behind the FSIA. First, the reasons for giving the assets of foreign central banks special treatment as regards prejudgment attachment—encouraging foreign central banks to maintain deposits in the United States and avoiding an adverse effect on United States foreign relations—apply with equal force to other court-ordered provisional remedies. Second, section 1602 of the FSIA, the findings and declaration of purpose section of the statute, refers to “determination[s] by United States courts” generally, and does not distinguish between particular remedies granted by United States courts. Third, the legislative history of section 1610(d) of the FSIA, which relates to prejudgment attachment of the property of a foreign state used for a commercial activity in the United States, suggests that section 1610(d) applies to all court-ordered provisional remedies used to prevent assets from being dissipated or removed from a jurisdiction to frustrate satisfaction of a judgment. By analogy, section 1611(b), which specifically addresses attachment of foreign central bank assets, should also apply to all court-ordered provisional remedies.

Despite the argument that prejudgment attachment should not be distinguished from other provisional remedies, a number of federal district courts outside of the Second Circuit, in cases involving claims against Iran (which arose during the 1979-80 “hostage crisis”), have nevertheless made such a distinction. Perhaps largely because of the political context in which they arose, these courts held that such other provisional remedies *are* permitted under the FSIA.<sup>166</sup> The reasoning

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<sup>163</sup> *S & S Mach. Co. v. Masinexportimport*, 706 F.2d 411, 418 (2d Cir. 1983), *cert. denied*, 464 U.S. 850 (1983). A New York state trial court in Manhattan has come to the same conclusion. *See Raji v. Bank Sepah-Iran*, 131 Misc. 2d 158, 495 N.Y.S.2d 576, 581 (Sup. Ct. 1985) (because the Iranian bank had not waived immunity from prejudgment attachment under section 1610(d), the court was barred by FSIA from granting an injunction, as well as an order for prejudgment attachment).

<sup>164</sup> 706 F.2d 411.

<sup>165</sup> 131 Misc. 2d 158, 495 N.Y.S.2d 576.

<sup>166</sup> *See American Int'l Group, Inc. v. Islamic Republic of Iran*, 657 F.2d 430 (D.C. Cir. 1981) (preliminary injunction granted to prevent removal of Iranian government assets from United States in case claiming expropriation of property located in Iran); *Pfizer v. Islamic Republic of Iran*, No. 80-2791 (D.D.C. Nov. 26, 1980) (FSIA

of these cases has not been followed to date, and it is not clear whether courts will do so in the future, absent an unusual political context such as that in which the Iranian cases arose. In any event, in any suit brought in a federal court in New York, Second Circuit precedent would be controlling on procedural issues, such as attachment and injunction. The assets of a central bank on deposit with the FRBNY or a commercial bank should therefore be immune from preliminary injunctions or temporary restraining orders to the extent that such assets would enjoy immunity from prejudgment attachment.

### 3.4.2. *Bank's Right of Set-Off*

In addition to the remedies discussed above, a creditor bank may be able to unilaterally set off deposits it holds in the name of a debtor and apply them against sums due to such bank from that debtor under its debt agreements.<sup>167</sup> Although there is no case law on point, it is far from clear that a court would find the FSIA to be a bar against any right of set-off which a creditor could otherwise assert against the foreign sovereign borrower. The FSIA by its terms does not confer any explicit immunity from set-off for assets held in the United States by either foreign states generally or by foreign central banks in particular, nor does the statute explicitly mention set-off. However, section 1607(c) of the FSIA and its legislative history indicate that in enacting the FSIA, Congress was aware of banks' traditional set-off rights and wished to preserve those rights unencumbered by sovereign immunity claims. Accordingly, section 1607(c) provides that United States courts will not grant immunity to foreign states with respect to a counterclaim "to the extent that the counterclaim does not seek relief exceeding in amount or differing in kind from that sought by the foreign state."<sup>168</sup>

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does not bar courts from ordering preliminary injunctions which differ from prejudgment attachments in that they run against persons and not property); *Electronic Data Sys. Corp. Iran v. Social Sec. Org. of Iran*, No. CA3-79-218-F (N.D. Tex. June 21, 1979) (preliminary injunction granted for equitable reason of preventing meaningless judgment and because preliminary injunction, unlike prejudgment attachment, does not purport to confer property rights); *Chas. T. Main Int'l, Inc. v. Khuzestan Water & Power Auth.*, No. 79-2304-C (D. Mass. Dec. 7, 1979) (court rejected claim that FSIA limits its inherent injunctive powers and granted preliminary injunction preventing disposition of defendant's U.S. property in case claiming non-payment for services).

<sup>167</sup> In New York, the only prerequisite to exercise of the right of set-off (which can arise under common law, contract or statute) is the giving of notice to the depositor pursuant to section 9-g of the New York Banking Law. N.Y. BANKING LAW § 9-g (McKinney Supp. 1988). The notice may be given by mail prior to or on the same day that the set-off occurs, and need only notify the depositor of the exercise of the right of set-off and state the reason therefor. Therefore, as a practical matter, such notice would be received by the depositor only after a bank has exercised its right of set-off.

<sup>168</sup> 28 U.S.C. § 1607(c) (1988).

The legislative history of section 1607(c) indicates that this provision was designed to "codif[y] the rule enunciated [by the United States Supreme Court] in *National City Bank v. Republic of China*."<sup>169</sup> In that case, China sued a United States bank for \$200,000 in deposits that the bank had refused to pay to China because the bank had used the deposit to set-off \$1.6 million in defaulted Chinese treasury notes. The Supreme Court upheld the set-off, holding that the bank's counterclaim, up to the amount of China's claim, was not barred by China's assertion of sovereign immunity.<sup>170</sup>

Notwithstanding section 1607(c)'s recognition of counterclaims, it might be argued that the importance to the United States government of foreign central banks' confidence in the sanctity of their United States-based deposits requires that special status be accorded to central banks in the context of set-off as well as in that of prejudgment attachment and other provisional remedies.<sup>171</sup> The argument may fail, however, given the express language of section 1607(c) and its legislative history, which explicitly permit set-off. Moreover, the federal court for the Eastern District of Louisiana, in *De Sanchez v. Banco Central de Nicaragua*,<sup>172</sup> held that the special treatment afforded to foreign central banks under section 1611(b) did not immunize the Nicaraguan central bank from suit under sections 1605(a)(3) and 1605(a)(5) of the FSIA.<sup>173</sup> Courts would be likely to apply this principle by analogy and find that, notwithstanding the importance to the United States government of foreign central banks' confidence in the immunity of their United States deposits, the special protection afforded by section 1611(b) against prejudgment attachment does not extend to set-off under section 1607(c).

This conclusion also follows from the fact that set-off is a self-help remedy that does not involve United States courts and, accordingly, is less likely to provoke foreign relations problems than court-ordered provisional remedies such as prejudgment attachment. In sum, there-

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<sup>169</sup> H.R. REP. NO. 1487, 94th Cong., 2d Sess., reprinted in 1976 U.S. CODE CONG. & ADMIN. NEWS 6604, 6622 (citations omitted).

<sup>170</sup> *National City Bank v. Republic of China*, 348 U.S. 356, 363-66 (1955).

<sup>171</sup> As previously noted, the preservation of central banks' confidence in the invulnerability of their United States deposits was one of the principal reasons for shielding them from prejudgment attachment in section 1611(b). See *supra* note 158 and accompanying text.

<sup>172</sup> 515 F. Supp. 900, 914 n.14 (E.D. La. 1981), *aff'd*, 770 F.2d 1385 (5th Cir. 1985).

<sup>173</sup> Sections 1605(a)(3) and 1605(a)(5), respectively, are concerned with cases claiming expropriation of property by a foreign state and with tort actions against a foreign state in which the plaintiff seeks money damages. 28 U.S.C. §§ 1605(a)(3), 1605(a)(5) (1988).

fore, accounts of a central bank or other sovereign debtor may be subject to set-off exercised by its lender banks to the greater extent of either (1) New York State common or statutory law, or (2) any applicable set-off provisions in any agreements between the depositor and any lender.

In the event, however, that a bank or other lender engaged in a set-off which a court later found to be unjustified (for example, if the bank wrongfully set off assets of one entity against obligations of another obligor), the party against whom set-off was wrongfully exercised would have a clear right to recover the sums improperly set off.<sup>174</sup> In addition, although there is no New York law directly on point, those United States courts which have considered the issue have held or implied that a bank which wrongfully sets off debts owed to the bank against a depositor's deposits will be liable for all damages proximately caused by such wrongful set-off.

For example, the Court of Appeals for the Eighth Circuit held, in *Dockendorf v. Dakota County State Bank*,<sup>175</sup> that a jury was entitled to award consequential damages to the owner of a cattle ranch whose business and reputation were harmed as a result of the defendant's wrongful set-off of certain local funds against the plaintiff's deposit account with the bank. Similarly, a Massachusetts district court held, in *Spencer Cos. v. Chase Manhattan Bank, N.A.*,<sup>176</sup> that the plaintiff would be entitled to recover any damages it might be able to prove resulted from an improper set-off against plaintiff's deposits by the defendant bank.<sup>177</sup>

### 3.5. *Post-judgment Attachment or Execution*

As noted above, commercial assets of the defendant, including a central bank, would become susceptible to post-judgment attachment or execution after the expiration of a "reasonable period of time" following entry of any adverse judgment. For the period between the date of judgment and the expiration of a "reasonable period of time," prejudg-

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<sup>174</sup> See, e.g., *Appleton v. National Park Bank*, 211 A.D. 708, 208 N.Y.S. 228, 231 (1925), *aff'd*, 241 N.Y. 561, 150 N.E. 555 (1925).

<sup>175</sup> 673 F.2d 961, 967-68 (8th Cir. 1981).

<sup>176</sup> 81 Bankr. 194, 198-99 (D. Mass. 1987).

<sup>177</sup> See *Prudential Ins. Co. v. Curt Bullock Builders, Inc.*, 626 F. Supp. 159, 163 (N.D. Ill. 1985) (if the bank had no right of set-off, the resulting dishonor of plaintiff's checks was wrongful and liability would be imposed for damages proximately caused by the dishonor); *HBL Indus. v. Chase Manhattan Bank, N.A.*, 45 Bankr. 865, 868 (S.D.N.Y. 1985) (wrongful set-off is a tort for wrongful conversion and damages will be awarded if the plaintiff demonstrates a possessory interest in the converted property).

ment attachment would remain available to the extent previously discussed. All commercial assets of the defendant, including central bank assets "held for its own account" which are situated in the State of New York, would be attachable based on a judgment rendered in a court sitting in New York. Moreover, assets located elsewhere in the United States would become subject to attachment after the filing or registration of the judgment in the state where the assets are located. In addition, assets located outside the United States might well become subject to attachment under the laws of that jurisdiction in a suit to enforce the United States judgment. Conversely, in the event that an action were commenced in a foreign (*i.e.*, non-United States jurisdiction) and a judgment obtained therein, assets located in New York could become subject to attachment upon enforcement of the foreign court's judgment if the terms of the Uniform Foreign Country Money Judgments Recognition Act were met.<sup>178</sup>

#### 4. ATTACHMENT OF ASSETS OF OTHER PUBLIC SECTOR ENTITIES FOR OBLIGATIONS OF A BORROWER

The foregoing discussion of immunity of a foreign state's assets from attachment and the availability of alternative remedies assumes that the creditor seeking relief has a valid claim against the entity whose assets it is seeking to attach. However, state entities that are not parties to loan agreements may have significant assets in the United States to which a creditor may want to look to satisfy any judgment it is awarded. Therefore, the question arises whether, in the absence of a valid claim against a particular foreign public sector entity, a creditor of a foreign sovereign debtor could look to the assets of the central bank (assuming it is not a debtor) or to another public sector entity to satisfy its claim. In the ordinary course, the answer is that it most likely cannot look to these assets.

Courts in the United States will respect the independence of a separate legal entity, including a wholly-owned foreign state corporation, absent extraordinary circumstances.<sup>179</sup> For example, in *Letelier v. Republic of Chile*<sup>180</sup> and *Hercaire International, Inc. v. Argentina*,<sup>181</sup> the United States Courts of Appeals for the Second and Eleventh Circuits each held that the assets of a national airline company, wholly

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<sup>178</sup> N.Y. CIV. PRAC. L. & R. 5301-5309 (McKinney 1978 & Supp. 1989).

<sup>179</sup> *First Nat'l City Bank v. Banco Para el Comercio Exterior de Cuba*, 462 U.S. 611, 626-27 (1983).

<sup>180</sup> 748 F.2d 790, 793 (2d Cir. 1984), *cert. denied*, 471 U.S. 1125 (1985).

<sup>181</sup> 821 F.2d 559, 564-65 (11th Cir. 1987).

owned by a government, could not be attached to satisfy a judgment rendered against the government.

The limited circumstances under which United States courts will not respect the separate juridical entity of foreign state corporations are set forth in the leading case of *First National City Bank v. Banco Para el Comercio Exterior de Cuba* ("Bancec").<sup>182</sup> After stating that there is a presumption in favor of honoring the separate legal status of foreign state instrumentalities, the Supreme Court held that this presumption can only be overcome where (1) the "corporate entity is so extensively controlled by its [foreign sovereign] owner that a relationship of principal and agent is created," or (2) the separate corporate entity of a foreign instrumentality is abused to work fraud or injustice, or to defeat some overriding public policy.<sup>183</sup> The Court emphasized that this standard was not a "mechanical formula for determining the circumstances under which the normally separate juridical status of a government instrumentality is to be disregarded,"<sup>184</sup> and, in effect, held that such a decision can be made only by analyzing the peculiar facts of each case.

In the six years since *Bancec*, however, no court has upset the presumption of corporate separateness in order to allow for the satisfaction of claims against one debtor through the assets of another entity. Although there may be reasons why a court could treat a central bank differently from another public sector entity with respect to obligations of the government (*e.g.*, because it holds all of the government's liquid assets), in only one case has a court even considered whether to disregard the distinction between a government and its central bank.<sup>185</sup> In that case, the court, without the benefit of any significant analysis or any discussion of the differences between a central bank and other public sector entities, respected the presumption of independence set forth in *Bancec*.

Although the analysis will clearly turn on the particular facts in question, a court applying United States law should generally uphold the separate juridical status of a central bank under its local government's law and not routinely permit a creditor of the government to have recourse to a central bank's assets, including its reserves, to satisfy its claims against the government.<sup>186</sup> As to the first prong of the *Bancec*

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<sup>182</sup> 462 U.S. 611 (1983).

<sup>183</sup> *Id.* at 629-30.

<sup>184</sup> *Id.* at 633.

<sup>185</sup> *Minpeco, S.A. v. Hunt*, 686 F. Supp. 427, 437 (S.D.N.Y. 1988), *cert. denied*, 486 U.S. 1008 (1988).

<sup>186</sup> Under New York law, any debt owed to a debtor, whether incurred within or without the state, is subject to attachment. N.Y. CIV. PRAC. L. & R. 6202 (McKinney 1980); N.Y. CIV. PRAC. L. & R. 5201(a) (McKinney 1978). On that basis, a lender

test, despite the general supervisory control exercised by a government, central banks are not "so extensively controlled by [the government] that a relationship of principal and agent is created."<sup>187</sup> Although a government exercises general supervision over its central bank and typically appoints its board of directors, on a day-to-day basis a central bank operates independently of government control and respects the legal formalities of its separate juridical status, such as debiting and crediting the government's accounts for all transfers of funds.<sup>188</sup> As to the second prong of *Bancec*, it would not work a "fraud or injustice" to recognize a central bank's separate juridical status, since the government's creditors were aware of that status in negotiating any loan agreement.

## 5. CONCLUSION

The reader of this Article may have been struck by the number of legal issues raised and then given merely tentative and theoretical answers. Litigation under sovereign debt agreements has been rare, and therefore many of the issues that could arise in such actions do not have definitive answers. Where firm authority is lacking, we have presented our analysis of the resolution a New York state or federal court would be most likely to reach if and when actually confronted with one of these unanswered questions. But, until the courts face and resolve these

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may argue that it is entitled to attach the assets of a central bank to satisfy the lender's claim against a sovereign debtor because the central bank is presumably indebted to the sovereign debtor by virtue of the government's deposits with the central bank. However, this argument will most likely be rejected by New York courts. *See, e.g.,* *Smith v. Amherst Acres, Inc.*, 43 A.D.2d 792, 350 N.Y.S.2d 236, 237 (1973) (attempted levy on an asset owned by a third party owing a debt to debtor held to exceed creditor's power to reach property to satisfy judgment); *Save Way Oil Co. v. 284 E. Parkway Corp.*, 115 Misc. 2d 141, 453 N.Y.S.2d 554, 556 (Civ. Ct. 1982), *appeal dismissed*, 125 Misc. 2d 480, 480 N.Y.S.2d 718 (App. Term. 1984) (creditor only entitled to restrain money owed directly to debtor, and not entitled to restrain money owed to one who in turn is allegedly indebted to debtor).

In addition, as a general rule, a creditor may attach a bank account only at the particular branch at which the account is maintained or through the bank's main office. *Digitrex, Inc. v. Johnson*, 491 F. Supp. 66, 69 (S.D.N.Y. 1980); *Therm-X-Chemical & Oil Corp. v. Extebank*, 84 A.D.2d 787, 444 N.Y.S.2d 26, 27 (1981). Thus, under New York law, a sovereign debtor's account at a central bank may only be attached to the extent that a remedy is available under the law of the jurisdiction where the central bank is located.

<sup>187</sup> *Bancec*, 462 U.S. 611, 629 (1983).

<sup>188</sup> *See Hester Int'l Corp. v. Federal Republic of Nigeria*, 681 F. Supp. 371, 380-81 (N.D. Miss. 1988), *aff'd*, 879 F.2d 170 (5th Cir. 1989) (wholly-owned Nigerian corporation not an alter-ego or agent of Republic of Nigeria and therefore not liable for the acts of the Republic). *See also Hercaire Int'l, Inc. v. Argentina*, 821 F.2d 559, 564-65 (11th Cir. 1987); *Letelier v. Republic of Chile*, 748 F.2d 790, 793 (2d Cir. 1984), *cert. denied*, 471 U.S. 1125 (1985).

issues, our answers must remain merely speculative; and we conclude this Article with the hope that there may continue to be no need for the courts to prove us right or wrong.