

A LEGAL REGIME FOR STATE-OWNED COMPANIES IN THE MODERN ERA

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*Foreign state-owned companies (SOCs), particularly those in the energy sector, are more powerful than ever before. Yet under the Foreign Sovereign Immunities Act of 1976 (FSIA), agencies and instrumentalities—a category in which many SOCs fall—enjoy a presumption of immunity. At the same time, however, pursuant to the U.S. Supreme Court’s 1983 decision in *First National City Bank v. Banco Para el Comercio Exterior de Cuba*, in most cases the foreign state also enjoys the benefit of legal separateness—i.e., it is very difficult for a third party to “pierce the corporate veil” between the sovereign and its subsidiary. Thus, SOCs enjoy immunity (a principle applied to sovereigns) while their parent governments are not responsible for the obligations of the SOCs (a principle more typically applied to traditional companies). In the author’s view, there is a significant underlying tension in such cases that gives one pause in an era of dominant SOCs.*

Over thirty years following the enactment of the FSIA, it is appropriate to re-examine the legal regime applicable to SOCs. In addition to the issues outlined above, there is significant confusion in the courts with respect to when an SOC is considered an agency or instrumentality and thus is entitled to a presumption of immunity. This Article proposes amendments to the FSIA in order to provide a more predictable and just legal regime for application to SOCs. In particular, the proposed amendments would involve eliminating immunity for agencies and instrumentalities altogether and revising the definition of foreign state to include specific types of entities, as well as other entities that engage in essentially public, non-commercial activity.

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INTRODUCTION

Foreign state-owned companies (SOCs), particularly those in the energy sector, are more powerful than ever before. There is no question that traditional companies remain powerful; ExxonMobil's second quarter 2008 profits reached nearly \$12 billion.¹ But the grand majority of worldwide oil reserves are controlled and exploited by state-owned oil companies.² In many cases these companies are sophisticated international market players, selling receivables, investing abroad, acquiring foreign subsidiaries, and issuing bonds while trading their products around the world. A recent study found that SOCs in the petroleum sector "want to operate like [international oil companies], though they are clearly national companies with public ownership of capital, special status in the hydrocarbon domain, obligations to the national market and a common history."³

Despite their commercial characteristics, SOCs are commonly provided with presumptive immunity from U.S. legal proceedings as "agencies or instrumentalities" of the foreign state under the Foreign Sovereign Immunities Act of 1976 (FSIA).⁴ Additionally, SOCs and their sovereign parents enjoy the shield of separate corporate status. This dual protection has created significant doctrinal tension and tilted the commercial playing field in favor of SOCs. The fact that immunity is also applied in an inconsistent and unpredictable manner has made the need for reform to ease this tension all the more apparent.

Therefore, this Article will propose a simple, straightforward way to modernize the FSIA by amendment. Specifically, the definition of "foreign state" should be broadened and clarified to list explicitly defense ministries, central banks, and the like as inherently part of the foreign state. Those falling within this definition would enjoy the benefit of immunity, but they would also typically be considered one and the same as the foreign state with respect to liability. Additionally, the term "agencies and instrumentalities"

1. Clifford Krauss, *Exxon's Second-Quarter Earnings Set a Record*, N.Y. TIMES, Aug. 1, 2008, at C2.

2. Tina Rosenberg, *The Perils of Petrocracy*, N.Y. TIMES MAGAZINE, Nov. 4, 2007, at 42 ("77 percent of the world's oil reserves are held by national oil companies with no private equity, and there are 13 [SOCs] with more reserves than ExxonMobil, the largest multinational oil company").

3. VALÉRIE MARCEL, *OIL TITANS 55* (Chatham House/Brookings Inst. Press, 2006).

4. Foreign Sovereign Immunities Act of 1976, 28 U.S.C. §§ 1330, 1441, 1602-1611 (2000 & Supp. V 2005).

should be eliminated from the definition of “foreign state” provided in 28 U.S.C. § 1603(a). SOCs will enjoy legal separateness, as they should, but due to their commercial, non-political nature, they should not be immune.

The proposed amendment to 28 U.S.C. § 1603(a) is as follows:

- (a) A “foreign state” includes the following:
- (1) the central government and its embassies, consulates and other diplomatic facilities abroad;
 - (2) all political subdivisions, including states, provinces, cities and other regional and local subdivisions;
 - (3) all state entities, agencies and offices whose principal, fundamental purpose and activity is public, rather than commercial, in nature, including departments, ministries, the armed services, regulatory agencies and other such entities, agencies and offices of the central government and its political subdivisions; and
 - (4) the central bank of that foreign state.

Not only are these reforms sensible, yielding more equitable results, but they would also provide needed simplification and clarity to the rules governing the liability of foreign states and their corporate subsidiaries. Foreign states would enjoy the benefits of a more predictable system, enabling them to conduct their governmental functions and structure their business operations accordingly. Moreover, other companies that do business with SOCs would also benefit by having a better understanding of when immunity could apply.

Part I of this Article will provide a discussion of the background of the FSIA more generally, with a particular focus on the distinctions among foreign states, political subdivisions, agencies and instrumentalities, and entities that do not fall within any of these categories. Part II will discuss *Bancec*⁵ and its application by the courts. Part III analyzes the tensions that are caused by the current rules of state liability due to the peculiarities of the application of those rules, while also examining the role that SOCs play in the modern business environment. Finally, Part IV offers a solution.

5. First Nat'l City Bank v. Banco Para El Comercio Exterior de Cuba, 462 U.S. 611 (1983).

I. THE DISTINCT SOVEREIGN ENTITIES FALLING WITHIN THE FSIA

A. *Brief Overview of the FSIA*

1. Historical Basis for Sovereign Immunity in the United States

Sovereign immunity arose based upon the principle that the ability of a foreign state to exercise its sovereignty without undue external interference must be protected.⁶ In other words, states (and the courts of those states) should refrain from entertaining legal actions against foreign sovereigns, based upon international comity.⁷ In reliance on this principle, throughout most of the United States' existence as a nation, U.S. courts have considered foreign sovereigns to be absolutely immune from their jurisdiction⁸ based upon the Supreme Court's 1812 decision in *The Schooner Exchange v. McFaddon*.⁹

In the 1940s, the Supreme Court began to consider as a significant factor in its immunity analysis whether the U.S. State Department had recommended that U.S. courts apply immunity in a particular case.¹⁰ In 1952, the U.S. State Department Acting Legal Advisor, Jack B. Tate, issued a letter to the Department of Justice (this letter would come to be known as the "Tate letter") announcing that the State Department had adopted the restrictive theory of sovereign immunity.¹¹ The restrictive theory holds that foreign sovereigns should not enjoy immunity for their commercial acts.¹²

The Tate letter left the Executive Branch with significant influence over courts' decisions, which led to unpredictable and inconsistent application by courts of the restrictive theory. In some cases, the Executive Branch would intervene, recommending to a court that immunity should apply in a particular instance. In other

6. See David P. Vandenberg, Comment, *In the Wake of Republic of Austria v. Altmann: The Current Status of Foreign Sovereign Immunity in United States Courts*, 77 U. COLO. L. REV. 739, 740 (2006).

7. *Id.* at 740-41.

8. See, e.g., *Berizzi Bros. Co. v. S.S. Pesaro*, 271 U.S. 562 (1926) (applying absolute immunity).

9. 11 U.S. 116 (1812). In a case brought by owners of a ship seized by the French Navy in Philadelphia Harbor, Chief Justice Marshall held that in the spirit of "equal rights and equal independence" of foreign sovereigns, courts typically must refrain from exercising jurisdiction over them. *Id.* at 136, 146.

10. See *Republic of Mex v. Hoffman*, 324 U.S. 30 (1945); *Ex Parte Republic of Peru*, 318 U.S. 578 (1943).

11. Letter from Jack B. Tate, Acting Legal Advisor for the Secretary of State, to Philip B. Perlman, Acting Attorney General (May 19, 1952), in *Changed Policy Concerning the Granting of Sovereign Immunity to Foreign Governments*, 26 DEP'T ST. BULL. 969, 984-85 (1952).

12. See *id.*

cases the Executive Branch would be silent, leaving a court to wonder how it should proceed. The result was the inconsistent application of an unclear rule.¹³

In 1976, Congress succeeded in codifying the restrictive theory in a comprehensive statutory scheme known as the Foreign Sovereign Immunities Act of 1976 (FSIA).¹⁴ The FSIA was enacted to accomplish four objectives: (1) codifying the restrictive theory of sovereign immunity; (2) ensuring that immunity became a judicial (rather than executive) determination; (3) providing a statutory procedure for serving foreign states; and (4) providing a remedy for a plaintiff against a noncompliant foreign sovereign judgment debtor.¹⁵ The hope was that the FSIA would resolve “considerable uncertainty” for both private litigants and foreign states.¹⁶

2. Basic Structure of the FSIA

The enactment of the FSIA did not create an independent federal cause of action,¹⁷ but rather established the exclusive jurisdictional statute for actions against foreign states.¹⁸ The basic structure of the FSIA begins with Sections 1604 and 1609, which provide the general rule of immunity.¹⁹ Section 1604 provides that foreign states are “immune from the jurisdiction of the courts of the United States and of the States except as provided in sections 1605 to 1607 of this chapter.”²⁰ Section 1609, meanwhile, provides that “the property in the United States of a foreign state shall be immune from attachment arrest and execution except as provided in sections 1610 and 1611 of this chapter.”²¹

Section 1605 provides a list of exceptions to the general rule of immunity from jurisdiction.²² A full examination of the exceptions would entail a lengthy discussion on its own, but for the purposes of this Article, it is sufficient to note that they include waiver, commercial activity, and cases involving any of the following:

13. H.R. REP. NO. 94-1487, at 8-9 (1976), *as reprinted in* 1976 U.S.C.C.A.N. 6604, 6606-07.

14. Foreign Sovereign Immunities Act of 1976, Pub. L. No. 94-583, 90 Stat. 2891, 2891-98 (codified as amended at 28 U.S.C. §§ 1330, 1441, 1602-1611 (2000)).

15. H.R. REP. NO. 94-1487, at 7-8, 1976 U.S.C.C.A.N. 6604, 6604-06.

16. H.R. REP. NO. 94-1487, at 6-9, 1976 U.S.C.C.A.N. 6604, 6604-07.

17. *Boxer v. Gottlieb*, 652 F. Supp. 1056, 1060 (S.D.N.Y. 1987); *Unidyne Corp. v. Gov't of Iran*, 512 F. Supp. 705, 709 (E.D. Va. 1981).

18. *City of N.Y. v. Permanent Mission of India to the U.N.*, 446 F.3d 365, 369 (2d Cir. 2006).

19. Foreign Sovereign Immunities Act of 1976, 28 U.S.C. §§ 1604, 1609 (2000).

20. *Id.* § 1604.

21. 28 U.S.C. § 1609.

22. *Id.* § 1605 (2000 & Supp. V 2005).

rights in property taken in violation of international law; rights in U.S. immovable property or other U.S. property acquired by succession or gift; money damages sought against a foreign state for injury occurring in the U.S.; actions to enforce agreements to arbitrate or confirm arbitral awards;²³ and in Section 1605A, added to the FSIA in 2008, money damages sought for injury caused by acts of terrorism.²⁴

Meanwhile, Section 1610 provides the main exceptions to immunity from execution or attachment.²⁵ Once again put simply, the property of a foreign state is not immune from execution or attachment if the property is located in the U.S., the property is used for a commercial activity in the U.S., and one of seven conditions applies: (1) waiver; (2) the property was used for the commercial activity upon which the claim is based; (3) the execution relates to a judgment establishing rights in property taken in violation of international law; (4) the execution relates to a judgment establishing rights in immovable property or property acquired by succession or gift; (5) the property consists of certain types of insurance policies; (6) the judgment is based on an order confirming an arbitral award; (7) or the judgment relates to an act of terrorism.²⁶ Additional exceptions to immunity from execution or attachment apply for agencies and instrumentalities.²⁷ Most importantly, it need not be established that the particular property at issue has been used for “commercial activity” in the U.S., but rather only that the agency or instrumentality generally engages in commercial activity in the U.S.²⁸ Meanwhile, Section 1611 provides additional protections for property owned by foreign central banks.²⁹

Under this statutory scheme, the burden of proof typically applies as follows: (1) the defendant must make a *prima facie* showing that it is a foreign state; (2) the plaintiff must demonstrate that an exception to immunity applies; and (3) the ultimate burden of proof on demonstrating immunity lies with the defendant.³⁰

While other provisions of the FSIA address such matters as the mechanics of subject-matter and personal jurisdiction,³¹ removability from state courts,³² punitive damages,³³ counterclaims³⁴ and

23. *Id.* § 1605(a).

24. National Defense Authorization Act for Fiscal Year 2008, Pub. L. No. 110-181, § 1083, 122 Stat. 337, 338-44 (2008) (to be codified at 28 U.S.C. § 1605A).

25. 28 U.S.C. § 1610 (2000 & Supp. V 2005).

26. *Id.* § 1610(a).

27. *Id.* § 1610(b).

28. *Id.*

29. *Id.* § 1611(b)(1).

30. *Kelly v. Syria Shell Petroleum Dev. B.V.*, 213 F.3d 841, 847 (5th Cir. 2000).

31. 28 U.S.C. § 1330 (2000).

32. *Id.* § 1441.

service of process,³⁵ the fundamental structure of the FSIA (including immunity and the exceptions thereto) is outlined above.

*B. Classifications of Foreign States and Their Subsidiaries
Under the FSIA*

The most important FSIA provisions for the purposes of this Article, however, delineate which entities fall within the scope of the FSIA. Sovereigns are generally quite sophisticated, and they tend to structure their operations in a complex manner. There are ministries, departments, sub-departments, offices, and various layers of subsidiaries. The question arises as to which of these entities falls within the scope of the FSIA.

Section 1603, the definitional section of the FSIA, provides the framework for this analysis:

- (a) [a] “foreign state” . . . includes a political subdivision of a foreign state or an agency or instrumentality of a foreign state as defined in subsection (b).
- (b) [a]n “agency or instrumentality of a foreign state” means any entity—
 - (1) which is a separate legal person, corporate or otherwise, and
 - (2) which is an organ of a foreign state or political subdivision thereof, or a majority of whose shares or other ownership interest is owned by a foreign state or political subdivision thereof, and
 - (3) which is neither a citizen of a State of the United States . . . nor created under the laws of any third country.³⁶

In other words, a “foreign state” includes not only a foreign sovereign as typically formulated—the United Republic of Tanzania, for example—but also all political subdivisions, agencies, and instrumentalities of the sovereign.

1. The Foreign State Proper and Political Subdivisions

There is no doubt that the United Republic of Tanzania and its U.S. embassy are each considered a “foreign state” under the

33. *Id.* § 1606.

34. *Id.* § 1607.

35. *Id.* § 1608.

36. 28 U.S.C. § 1603 (2000 & Supp. V 2005).

FSIA; the embassy is the state itself, acting as an arm of the state in the U.S. Each of these entities could be considered the “foreign state proper.” Meanwhile, political subdivisions, agencies, and instrumentalities are not part of the foreign state proper but are considered to be “foreign states” under the FSIA.

The term “political subdivision” is not defined in the FSIA. The legislative history indicates that the term was intended to include “all governmental units beneath the central government, including local governments.”³⁷ True to this description, courts have found, for example, the Argentine province of Formosa,³⁸ the Nigerian state of Cross River³⁹ and the city of Amsterdam⁴⁰ to be political subdivisions under the FSIA.

2. Agencies and Instrumentalities

Application of the FSIA to agencies and instrumentalities involves a more complex analysis. Agencies and instrumentalities (terms between which courts do not distinguish, but rather consider to be synonymous) must meet the three criteria outlined in Section 1603(b).⁴¹ Typically the first and third criteria involve a straightforward determination. The first criterion requires that the entity be “a separate legal person, corporate or otherwise.”⁴² According to the legislative history, this “is intended to include a corporation, association, foundation, or any other entity which, under the law of the foreign state where it was created, can sue or be sued in its own name, contract in its own name or hold property in its own name.”⁴³ It is usually not difficult to determine whether an entity is a separate legal person for the purposes of this definition.

The third criterion is that the entity must be “neither a citizen of a State of the United States . . . nor created under the laws of any third country.”⁴⁴ As explained in the legislative history, “[t]he rationale behind these exclusions is that if a foreign state acquires or establishes a company or other legal entity in a foreign country, such entity is presumptively engaging in activities that are either

37. H.R. REP. NO. 94-1487, at 15 (1976), *as reprinted in* 1976 U.S.C.C.A.N. 6604, 6613.

38. *Wasserstein Perella Emerging Mkts. Fin., L.P. v. Province of Formosa*, No. 97 CIV. 793(BSJ), 2002 WL 1453831, at *7 (S.D.N.Y., July 2, 2002).

39. *Hester Int'l Corp. v. Fed. Republic of Nig.*, 681 F. Supp. 371, 377 (N.D. Miss. 1988), *aff'd*, 879 F.2d 170 (5th Cir. 1989).

40. *Malewicz v. City of Amsterdam*, 362 F. Supp. 2d 298, 306 (D.D.C. 2005).

41. 28 U.S.C. § 1603(b) (2000).

42. *Id.* § 1603(b)(1).

43. H.R. REP. NO. 94-1487, at 15 (1976), *as reprinted in* 1976 U.S.C.C.A.N. 6604, 6614.

44. 28 U.S.C. § 1603(b)(3) (2000).

commercial or private in nature.”⁴⁵ Again, it is straightforward to determine whether an entity was created under the laws of the foreign state, or rather of a third country.

The second criterion, on the other hand, has tended to be more difficult in application for courts. There are two ways that an entity can qualify as an agency or instrumentality under Section 1603(b)(2): either it “is an organ of a foreign state or political subdivision thereof, or a majority of [its] shares or other ownership interest is owned by a foreign state or political subdivision thereof.”⁴⁶

Typically a court will apply the majority ownership prong first, as this analysis tends to be more straightforward than that for the organ prong. Prior to 2003, some courts had considered indirect subsidiaries of a foreign state proper to be “majority . . . owned by a foreign state.”⁴⁷ In *Dole Food Co. v. Patrickson*, decided by the U.S. Supreme Court in 2003, the Court settled once and for all the question whether majority ownership needed to be direct, or rather if an entity held indirectly by the foreign state (i.e., with one or more layers in the corporate ownership chain between the foreign state and the entity) would also qualify as majority-owned under Section 1603(b)(2).⁴⁸

In *Dole*, a group of workers from several Latin American countries filed suit against their employer Dole Food Company, alleging injuries from exposure to chemicals.⁴⁹ Dole impleaded two chemical manufacturers indirectly owned by the State of Israel.⁵⁰ The Court found that the companies at issue, which were

separated from the State of Israel by one or more intermediate corporate tiers . . . cannot come within the statutory language which grants status as an instrumentality of a foreign state to an entity a “majority of whose shares or other ownership interest is owned by a foreign state or political subdivision thereof.” We hold that only direct ownership of a majority of shares by the foreign state satisfies the

45. H.R. REP. NO. 94-1487, at 15.

46. 28 U.S.C. § 1603(b)(2) (2000) (emphasis added).

47. See *In re Air Crash Disaster Near Roselawn*, 96 F.3d 932, 939-41 (7th Cir. 1996); cf. *Gates v. Victor Fine Foods*, 54 F.3d 1457, 1461-63 (9th Cir. 1995). In other words, the argument would be that because the FSIA considers an agency or instrumentality to be a “foreign state,” an entity that is majority-owned by an agency or instrumentality is majority-owned by a foreign state, thus itself falling with the definition of agency or instrumentality.

48. 538 U.S. 468, 474-78 (2003).

49. *Id.* at 471.

50. *Id.*

statutory requirement.⁵¹

In a case where the foreign state is not a direct majority owner of the entity, the entity attempting to establish immunity must turn to the other prong of Section 1605(b)(2) and demonstrate that it is an organ of the state. The various U.S. Courts of Appeal have established similar tests to determine whether an entity is an organ of the state. The Second Circuit, for example, considers the following:

- (1) whether the foreign state created the entity for a national purpose;
- (2) whether the foreign state actively supervises the entity;
- (3) whether the foreign state requires the hiring of public employees and pays their salaries;
- (4) whether the entity holds exclusive rights to some right in the [foreign] country; and
- (5) how the entity is treated under foreign state law.⁵²

The Fifth Circuit applies an identical test, while the test applied by the Third Circuit is very similar.⁵³ While these tests may differ subtly, the heart of the analysis in each case revolves around the purpose for which the entity was established and the degree of control that the state exercises over the entity.

C. *Determining Among the Three Possibilities*

There are several significant differences in treatment under the FSIA depending upon whether an entity is a foreign state proper or political subdivision, on the one hand, or an agency or instrumentality on the other. For example, only agencies or in-

51. *Id.* at 473-74 (quoting § 1603(b)(2)).

52. *Filler v. Hanvit Bank*, 378 F.3d 213, 217 (2d Cir. 2004) (alteration in original) (quoting *Kelly v. Syria Shell Petroleum Dev.*, 213 F.3d 841, 846-47 (5th Cir. 2000)).

53. *USX Corp. v. Adriatic Ins. Co.*, 345 F.3d 190, 209 (3d Cir. 2003) (considering “(1) the circumstances surrounding the entity’s creation; (2) the purpose of its activities; (3) the degree of supervision by the government; (4) the level of government financial support; (5) the entity’s employment policies, particularly regarding whether the foreign state requires the hiring of public employees and pays their salaries; (6) the entity’s obligations and privileges under the foreign state’s laws,” and adding “(7) the ownership structure of the entity.”); *Kelly*, 213 F.3d at 846-47 (5th Cir. 2000) (applying the same test as that used by the Second Circuit) (quoting *Supra Med. Corp. v. McGonigle*, 955 F. Supp. 374, 379 (E.D. Pa. 1997)).

strumentalities may be subject to punitive damages.⁵⁴ Additionally, service requirements are less demanding for agencies and instrumentalities than for foreign states proper or political subdivisions.⁵⁵ Venue in the U.S. District Court for the District of Columbia is automatically appropriate for foreign states proper or political subdivisions, but not necessarily so for agencies and instrumentalities.⁵⁶ Finally, and perhaps most importantly, the exceptions to immunity from attachment or execution are broader for agencies and instrumentalities than for foreign states proper or political subdivisions.⁵⁷

Thus, even if an entity will be covered by the FSIA regardless, it is legally significant to distinguish between these categories of entities that fall under the umbrella of the FSIA. This question would arise, for example, when an entity meets the criteria for agency or instrumentality status, but claims to be a foreign state proper. The legislative history provides that

[a]s a general matter, entities which meet the definition of "agency or instrumentality of a foreign state" could assume a variety of forms, including a state trading corporation, a mining enterprise, a transport organization such as a shipping line or airline, a steel company, a central bank, an export association, a governmental procurement agency or a department or ministry which acts and is suable in its own name.⁵⁸

Quite unhelpfully, this list of examples would seem to include a number of entities, such as departments, ministries and central banks, that most would consider to be part of the foreign state proper.⁵⁹

The courts have adopted two tests to distinguish between the two types of entities: a "legal characteristics test" and a "core function" test. The core function test examines whether the core function of the entity is commercial; if it is, the entity is considered to be an agency or instrumentality.⁶⁰ The legal characteristics test, meanwhile, examines whether, under the law of the foreign state where it was created, the entity can sue and be sued, own proper-

54. 28 U.S.C. § 1606 (2000).

55. *Id.* § 1608.

56. *Id.* § 1391(f)(3)-(4).

57. *Id.* § 1610.

58. H.R. REP. NO. 94-1487, at 15-16 (1976), as reprinted in U.S.C.C.A.N. 6604, 6614.

59. Working Group of the Am. Bar Ass'n, *Reforming the Foreign Sovereign Immunities Act*, 40 COLUM. J. TRANSNAT'L L. 489, 509-10 (2002).

60. *Transaero, Inc. v. La Fuerza Aerea Boliviana*, 30 F.3d 148, 151 (D.C. Cir. 1994).

ty, and contract, all in its own name; if so, the entity is considered an agency or instrumentality.⁶¹ Typically, courts apply one test or the other.

II. PIERCING THE VEIL BETWEEN THE SOVEREIGN AND ITS SUBSIDIARY: *BANCEC*

A. *The Bancec Presumption of Separateness*

A separate, yet inextricably intertwined question relates to when a foreign state may be held responsible for the actions or obligations of its subsidiary, or vice versa. This question commonly arises with respect to execution or attachment, where the plaintiff seeks to collect on a judgment against a foreign state by executing upon the assets of the state's subsidiary. The issue would also exist where a plaintiff seeks to impute the commercial activity of an SOC to the parent government for the purposes of establishing an exception to sovereign immunity.

The seminal case in this context is *First National City Bank v. Banco Para El Comercio Exterior de Cuba (Bancec)*, decided by the U.S. Supreme Court in 1983.⁶² *Bancec* established a rebuttable presumption that "government instrumentalities established as juridical entities distinct and independent from their sovereign should normally be treated as such."⁶³ In stating this general rule, the Court quoted from the legislative history of the FSIA:

Section 1610(b) will not permit execution against the property of one agency or instrumentality to satisfy a judgment against another, unrelated agency or instrumentality. There are compelling reasons for this. If U.S. law did not respect the separate juridical identities of different agencies or instrumentalities, it might encourage foreign jurisdictions to disregard the juridical divisions between different U.S. corporations or between a U.S. corporation and its independent subsidiary.⁶⁴

The Court then stated that the presumption of legal separateness can be rebutted upon a showing either that: (1) the "corporate enti-

61. *Hyatt Corp. v. Stanton*, 945 F. Supp. 675, 681 (S.D.N.Y. 1996).

62. 462 U.S. 611 (1983).

63. *Id.* at 626-27.

64. *Id.* at 627-28 (quoting H.R. REP. NO. 94-1487, at 29-30 (1976), as reprinted in 1976 U.S.C.C.A.N. 6604, 6628-29).

ty is so extensively controlled by its owner that a relationship of principal and agent is created” (i.e., the parent is an alter ego of the corporation); or (2) recognition of the separate corporate status “would work fraud or injustice” on the other party.⁶⁵

B. *The Bancec Exceptions*

Under the principal/agent exception, a court will typically “pierce the corporate veil” only where it is established that the parent exercises day-to-day operational control over the subsidiary.⁶⁶ Meanwhile, the kind of control that any sole shareholder would normally exercise over its subsidiary is insufficient to justify piercing the veil.⁶⁷

Under the fraud or injustice exception, courts apply a fact-specific analysis to determine whether recognition of separate legal status would be unfair. Typically such cases involve the foreign state’s manipulation of the corporate form for its own benefit, to the detriment of the plaintiff.⁶⁸ The primary example here is *Bancec* itself.

Bancec, a Cuban government-owned bank utilized in foreign trade, attempted to collect on a letter of credit from First National City Bank (now Citibank) in U.S. court.⁶⁹ Citibank claimed a setoff based upon the Cuban expropriation of its assets, which was effected by Banco Nacional (the Cuban National Bank) and the Cuban government.⁷⁰ After filing the initial claim, *Bancec* was dissolved.⁷¹ Its assets, including the claim, were passed to the Cuban National Bank, and then to another entity shortly thereafter.⁷² The Supreme Court found that the fraud or injustice exception applied because: (1) due to the dissolution of *Bancec*, the Cuban government and Cuban National Bank would be the only beneficiaries of any recovery; and (2) if Cuba had brought the claim itself, it

65. *Id.* at 629. It should be noted that, following amendments to the FSIA in January 2008, *Bancec* does not apply to execution or attachment in terrorism cases. *See infra* note 213. Rather, in cases falling under Section 1605A of the FSIA, “the property of an agency or instrumentality of [a foreign state that is a judgment debtor for a claim based upon acts of terrorism], including property that is a separate juridical entity or is an interest held directly or indirectly in a separate juridical entity, is subject to attachment in aid of execution.” National Defense Authorization Act for Fiscal Year 2008, Pub. L. No. 110-181, § 1083, 122 Stat. 337, 341 (2008) (to be codified at 28 U.S.C. § 1610(g)(1)).

66. *See infra* text accompanying notes 94-95.

67. *See infra* text accompanying notes 96-98.

68. *See infra* Section III.B.2.

69. First Nat’l City Bank v. Banco Para El Comercio Exterior de Cuba, 462 U.S. 611, 613, 615 (1983).

70. *Id.* at 616.

71. *Id.*

72. *Id.* at 616, 632.

would have been subject to the counterclaim.⁷³ Cuba could not “reap the benefits of our courts while avoiding the obligations of international law.”⁷⁴ Thus, the Court “decline[d] to adhere blindly to the corporate form where doing so would cause such an injustice” and permitted the setoff.⁷⁵

Successfully piercing the corporate veil is a rare feat for those attempting to meet the exceptions established in *Bancec*. The cases establish that the degree of day-to-day operational control that a plaintiff must demonstrate to prove a principal/agent relationship is indeed extensive, and few are able to make this showing.⁷⁶ Moreover, the fraud or injustice exception applies rarely, and only in unique factual circumstances.⁷⁷

This sensible approach is how the Supreme Court intended it to be. As the Court noted in *Bancec*,

[f]reely ignoring the separate status of government instrumentalities would result in substantial uncertainty over whether an instrumentality’s assets would be diverted to satisfy a claim against the sovereign, and might thereby cause third parties to hesitate before extending credit to a government instrumentality without the government’s guarantee. As a result, the efforts of sovereign nations to structure their governmental activities in a manner deemed necessary to promote economic development and efficient administration would surely be frustrated.⁷⁸

Bancec is based upon sound legal principles, and its underlying policy rationale is well founded. While this Article proposes changes to the FSIA, the law governing corporate separateness with respect to SOCs is sensible and need not be changed.

73. *Id.* at 630-32.

74. *Id.* at 634.

75. *Id.* at 632.

76. See *infra* notes 94–98 and accompanying text.

77. See, e.g., *Bridas S.A.P.I.C. v. Turkmenistan*, 447 F.3d 411, 417 (5th Cir. 2006) (holding that the fraud and injustice exception was satisfied because the Turkmen government manipulated the corporate form in an attempt to shield itself from liability); *Banco Central de Reserva del Peru v. Riggs Nat’l Bank of Washington, D.C.*, 919 F. Supp 13, 16 (D.D.C. 1994) (where a Peruvian SOC had taken out a loan from an American bank and another Peruvian SOC provided an offsetting deposit, the court found that treating the entities as distinct would work a fraud or injustice, and permitted the setoff).

78. *First Nat’l City Bank v. Banco Para El Comercio Exterior de Cuba*, 462 U.S. 611, 626 (1983) (footnote omitted).

III. TENSIONS CAUSED BY THE CURRENT RULES GOVERNING STATE LIABILITY

The legal rules governing immunity for SOCs are a different story. Over thirty years after the enactment of the FSIA, the body of case law interpreting this statutory scheme—while reflecting a generally successful effort by Congress to render the application of immunity more predictable than it was previously—has yielded a considerable amount of confusion and doctrinal tension regarding the entities that fall within its ambit. Some confusion has arisen due to the Supreme Court’s 2003 decision in *Dole Food Co. v. Patrickson*.⁷⁹ More fundamentally, however, there is an underlying tension between the distinct standards for the “organ” analysis under Section 1603(b) of the FSIA and the principal/agent analysis under *Bancec*, creating a bizarre contradiction whereby a company and its sovereign owner enjoy the fundamentally corporate status of legal separateness along with the essentially sovereign status of immunity.

A. *The Impact of Dole Food Co. v. Patrickson*

As discussed in Section I.B.2 above, the Supreme Court in *Dole Food Co. v. Patrickson* held that “only direct ownership of a majority of shares by the foreign state satisfies the statutory requirement” involving an entity a “majority of whose shares or other ownership interest is owned by a foreign state or political subdivision thereof.”⁸⁰ The majority ownership prong was plainly the only one discussed by the Court; Dole had not argued explicitly that the companies at issue were organs of the state. The bulk of the Court’s opinion was quite clear that the reach of its ruling extended only to the majority ownership prong; in fact, the Court did not once mention the organ prong.

However, when the companies at issue asserted that Israel “exercised considerable control over their operations,” the Court found that “[m]ajority ownership by a foreign state, not control, is the benchmark of instrumentality status.”⁸¹ The Court went on to state that “[t]he statutory language will not support a control test that mandates inquiry in every case into the past details of a foreign nation’s relation to a corporate entity in which it does not own a majority of the shares”⁸²—in other words, precisely what the or-

79. 538 U.S. 468.

80. *Id.* at 474 (quoting § 1603(b)(2)).

81. *Id.* at 477.

82. *Id.*

gan test requires. Moreover, on the last page of its opinion the Court held that “a foreign state must itself own a majority of the shares of a corporation if the corporation is to be deemed an instrumentality of the state under the provisions of the FSIA.”⁸³

This statement suggests that *only* companies that are directly majority-owned by the state could qualify as agencies or instrumentalities, thus reading the organ prong right out of the statute. Contrary to this apparent implication, U.S. Courts of Appeal continue to apply the organ prong post-*Dole*; *Filler v. Hanvit Bank*,⁸⁴ decided by the Second Circuit in 2004, and *USX Corporation v. Adriatic Insurance Co.*,⁸⁵ decided by the Third Circuit in 2003, are two examples. However, the author can state, based on his own personal experience, that some practitioners remain under the impression—or feign to be so as it suits them in their pleadings—that direct majority ownership is the exclusive means to agency/instrumentality status.

Merely adding to the confusion, some courts in fact have interpreted *Dole* in this fashion. In *Allen v. Russian Federation*, decided by the U.S. District Court of the District of Columbia in November 2007, the court found that the plaintiffs’ argument that “Rosneft is an agency or instrumentality of the Russian Federation despite its status as an indirect subsidiary of the Russian Federation . . . is nothing more than a frontal assault on the Supreme Court’s decision in *Dole*.”⁸⁶ These are harsh words for an argument that has been accepted by numerous courts.

When the plaintiffs urged the court to pierce the corporate veil to treat Rosneft’s parent company Rosneftegaz (directly held by the Russian Federation) and the Russian Federation as a single entity, the court found that “[t]his argument . . . is simply an attempt to circumvent the *Dole* holding.”⁸⁷ At this point the author will forgive the reader if he or she feels dizzy. It would seem that the “considerable uncertainty” sought to be remedied by the enactment of the FSIA over thirty years ago is creeping back.⁸⁸

83. *Id.* at 480.

84. 378 F.3d 213, 217 (2d Cir. 2004).

85. 345 F.3d 190, 209 (3d Cir. 2003).

86. *Allen v. Russian Fed’n*, 522 F. Supp. 2d 167, 184 (D.D.C. 2007).

87. *Id.* at 184-85.

88. H.R. REP. NO. 94-1487, at 6-9, 1976 U.S.C.C.A.N. 6604, 6604-07.

B. The Underlying Tension Between Organ Status and Bancec

1. The Role of Sovereign States and Their Subsidiaries

A second, more fundamental problem relates to the underlying tension between the organ analysis under the agency/instrumentality formulation and the principal/agent analysis under *Bancec*.⁸⁹ Historically, sovereign immunity was a concept created to apply to foreign states proper. But states have become more sophisticated, structuring their commercial operations through legally separate entities that also enjoy immunity under the FSIA.

Meanwhile, the benefits of corporate separateness historically have applied to traditional companies and individuals who seek to compete in the marketplace. By creating a separate company, a company or individual can engage in a commercial venture without the worry of being held liable for that separate entity's obligations. This legal principle rightfully encourages and promotes investment, entrepreneurship and activity that fosters growth in a given country's—or increasingly, the interconnected world's—economy.

Sovereign states have been the most powerful entities in the world for some time. Their control of economic and other public policy, as well as their immense financial resources due to their unique power to tax their inhabitants, renders sovereign states advantageously and specially positioned to participate in the global economy. As the Supreme Court discussed in *Bancec*, the ability of sovereign states to utilize separate subsidiaries can have numerous positive effects on society:

Increasingly during this century, governments throughout the world have established separately constituted legal entities to perform a variety of tasks. The organization and control of these entities vary considerably, but many possess a number of common features. . . . These distinctive features permit government instrumentalities to manage their operations on an enterprise basis while granting them a greater degree of flexibility and independence from close political control than is generally enjoyed by government agencies. These same features fre-

89. *First National City Bank v. Banco Para El Comercio Exterior de Cuba (Bancec)*, 462 U.S. 611 (1983).

quently prompt governments in developing countries to establish separate juridical entities as the vehicles through which to obtain the financial resources needed to make large-scale national investments.⁹⁰

Foreign states, both developed and developing, utilize SOCs to implement important commercial goals and promote economic growth.

2. The Tension Between the Principal/Agent and Organ Standards

The case for the utility of separate corporate subsidiaries for foreign states is convincing, as is the principle that states should generally be insulated from the obligations of these subsidiaries. However, it is unconvincing that such entities, market players that they are, should enjoy a level of immunity similar to that of the foreign state proper. Indeed, a gap exists in the law that yields such a result; that gap is created by the fact that agency/instrumentality status and principal/agent status are based upon two different standards, resulting in numerous entities that enjoy both immunity, essentially a sovereign feature, and corporate separateness, which is essentially a private feature. This gap unjustly tilts the competitive playing field of the marketplace in the direction of sovereigns and their SOCs.

As discussed in further detail in Section I.B.2 above, relatively speaking, it is not very difficult to establish organ status. Essentially, the purpose of the entity should somehow be public, and the state must exert some reasonable amount of control over the entity.⁹¹ Under the *Bancec* standard, on the other hand, the control exercised by the state must be significant, rising to the level of day-to-day operational control.⁹² As described by the U.S. Court of

90. *Id.* at 624-25 (footnote omitted). According to the Court, [a] typical government instrumentality, if one can be said to exist, is created by an enabling statute that prescribes the powers and duties of the instrumentality, and specifies that it is to be managed by a board selected by the government in a manner consistent with the enabling law. The instrumentality is typically established as a separate juridical entity, with the powers to hold and sell property and to sue and be sued. Except for appropriations to provide capital or to cover losses, the instrumentality is primarily responsible for its own finances. The instrumentality is run as a distinct economic enterprise; often it is not subject to the same budgetary and personnel requirements with which government agencies must comply.

Id.

91. See *Filler v. Hanvit Bank*, 378 F.3d 213, 217 (2d Cir. 2004); see also note 53 and accompanying text.

92. *Bancec*, 462 U.S. at 614.

Appeals for the Fifth Circuit, despite the use of the term “agency” in both contexts, the *Bancec* analysis is a “completely different inquiry,” and “the level of state control required to establish an ‘alter ego’ relationship is more extensive than that required to establish FSIA ‘agency.’”⁹³

For example, when an Iranian cabinet minister became involved in the daily decision-making process of an SOC and the company was carrying out Iranian political (as opposed to commercial) policy, this constituted day-to-day operational control.⁹⁴ Additionally, when Brasoil (owned by Braspetro, which was owned by Petrobras) had no president, but its parent companies executed agreements on behalf of Brasoil, handled Brasoil’s legal work, made decisions at their headquarters regarding Brasoil’s day-to-day operations, and utilized Brasoil’s bank accounts in New York for their worldwide transactions, Petrobras exercised day-to-day operational control over Brasoil.⁹⁵

Such cases are anomalous. More typical was a case where the U.S. Court of Appeals for the Ninth Circuit found that proposing candidates for the board of directors, assisting “in the preparation of regulations, budgets, and reports on banking operations in Iran,” but no involvement in day-to-day operations, was insufficient to establish a principal/agent relationship.⁹⁶ Another example occurred when the U.S. Court of Appeals for the D.C. Circuit found that owning all stock, appointing the board of directors, financial infusion, and the approval of certain sales, while again lacking control of day-to-day operations, was also insufficient to establish a principal/agent relationship.⁹⁷ Finally, a last representative example occurred when the U.S. District Court for the Southern District of New York found that appointing the board of directors, a majority of whom are government employees, typifies all instrumentalities and their parent governments; the Court also found that the power of the government to decree the entity’s dissolution did not

93. *Hester Int’l Corp. v. Fed. Republic of Nig.*, 879 F.2d 170, 176 n.5 (5th Cir. 1989).

94. *McKesson Corp. v. Islamic Republic of Iran*, 52 F.3d 346, 352 (D.C. Cir. 1995).

95. *U.S. Fid. & Guar. Co. v. Braspetro Oil Servs. Co.*, No. 97 CIV. 6124(JGK), 1999 WL 307666, at *9 (S.D.N.Y. May 17, 1999); *U.S. Fid. & Guar. Co. v. Petroleo Brasileiro S.A.-Petrobras*, No. 98 CIV. 3099(JGK), 1999 WL 307642 (S.D.N.Y. May 17, 1999). These two cases were companion actions decided the same day. *See also* *Kalamazoo Spice Extraction Co. v. Provisional Military Gov’t of Socialist Eth.*, 616 F. Supp. 660, 666 (W.D. Mich. 1985) (the government exercised direct control over the company; all checks over \$25,000 needed approval by a government-appointed director; all invoices for shipments exceeding \$13,000 needed approval by a government agency).

96. *Flatow v. Islamic Republic of Iran*, 308 F.3d 1065, 1073 (9th Cir. 2002).

97. *Transamerica Leasing, Inc. v. La Republica de Venez.*, 200 F.3d 843, 851-52 (D.C. Cir. 2000).

establish a principal/agent relationship.⁹⁸ Piercing the corporate veil rarely occurs; more typically, separate legal status remains intact.

3. Specific Examples of Dual Protection

Thus, many cases arise where an SOC and its sovereign parent enjoy the dual protection of both corporate separateness and immunity. For example, in *Corporación Mexicana de Servicios Marítimos, S.A. de C.V. v. M/T Respect* (decided by the U.S. Court of Appeals for the Ninth Circuit in 1996), a dispute had arisen over a freight contract between Pemex-Refinación (“Pemex-Refining”) and a Mexican private corporation.⁹⁹ Pemex is the Mexican state-owned oil company.¹⁰⁰ In 1992, Pemex was restructured so that it became a holding company for four subsidiaries, each of which carried out a different part of the oil business.¹⁰¹ Pemex-Refining, as the name suggests, is responsible for the refining, manufacturing, and distribution of gasoline and other products.¹⁰²

The Ninth Circuit found that Pemex-Refining was an organ of the Mexican state.¹⁰³ Quoting from the court below, it noted that

[Pemex-Refining] is an integral part of the United Mexican States. Pemex[-Refining] was created by the Mexican Constitution, Federal Organic Law, and Presidential Proclamation; it is entirely owned by the Mexican Government; is controlled entirely by government appointees; employs only public servants; and is charged with the exclusive responsibility of refining and distributing Mexican government property.¹⁰⁴

The issue of piercing the corporate veil was not before the court, as

98. *Minpeco, S.A. v. Hunt*, 686 F. Supp. 427, 435-36 (S.D.N.Y. 1988).

99. 89 F.3d 650, 652.

100. *Id.* at 654.

101. *Id.*

102. *Id.*

103. *Id.* at 655.

104. *Id.* (quoting District Court opinion) (alteration in original). Other courts have found Pemex to be an agency or instrumentality under the FSIA. In *Stena Rederi AB v. Comision de Contratos del Comité Ejecutivo General*, 923 F.2d 380, 386 n.7 (5th Cir. 1990), the Fifth Circuit found that “[t]here is no question that Pemex is a ‘foreign state’ for purposes of the FSIA.” Similarly, in *Arriba Ltd. v. Petroleos Mexicanos*, 962 F.2d 528, 533 (5th Cir. 1992) (citing *Stena*, 923 F.2d), the U.S. Court of Appeals for the Fifth Circuit determined that Pemex’s status as a foreign government instrumentality was “undisputed,” without engaging in an organ or majority ownership analysis. In each case, the Court found that the plaintiff had failed to demonstrate the applicability of the commercial activity exception, so Pemex was immune from suit.

the plaintiff was not seeking to hold the Mexican government liable for Pemex-Refining's obligations under the contract. However, based upon the other cases discussed above, it is clear that the above facts would be insufficient to establish a principal/agent relationship between Pemex-Refining and the Mexican government.

Another example is presented by the U.S. Court of Appeals for the Fifth Circuit's decision in *Kelly v. Syria Shell Petroleum Development B.V.*¹⁰⁵ This case involved an action brought by the survivors of firefighters who had been killed by a fire caused by gas escaping from a well operated by the defendants.¹⁰⁶ The court noted that Al Furat Petroleum Company ("Al Furat"), a Syrian company owned 50% by Syrian Petroleum Company (an entity wholly owned by the Syrian government), 31.25% by Syria Shell, and 18.75% by Deminex Syria GmbH,

was formed pursuant to a government authorization decree stating that Al Furat's objective is to develop identified petroleum reserves in Development Lease Areas in Syria; its by-laws require that, for its eight-member board, four be appointed by Syrian Petroleum Company, with one always serving as chairman; and . . . Syrian Petroleum Company's representatives on the board have invariably been Syrian government officials representing the highest level of government.¹⁰⁷

The court concluded that Al Furat had established that it was an organ of the Syrian government.¹⁰⁸ Again, veil piercing was not at issue—the firefighters' survivors were not seeking compensation from the Syrian government—but the facts outlined above would seem insufficient to establish a principal/agent relationship.

Each of these cases involved state-owned oil companies that the FSIA provides with immunity, yet the state itself also enjoys the benefits of corporate separateness. The activities in which these entities engage are fundamentally commercial, yet they compete with other companies in the market with the benefit of presumed immunity. In an age when SOCs exert immense power and influence, their ability to assert immunity seems less appropriate with each passing day on which the price of a barrel of oil rises.

105. 213 F.3d 841 (5th Cir. 2000).

106. *Id.* at 844-45.

107. *Id.* at 847-48.

108. *Id.* at 849.

C. The Use of Subsidiaries by Sovereigns

SOCs, particularly those in the oil and gas industry, are increasingly influential. The far-reaching power of the Standard Oil Trust, followed by the dominance of its former constituent parts that begot Exxon, Mobil, Chevron and others, long ago ceded control of much of the world's oil reserves to host governments.¹⁰⁹ Not only do SOC's control the vast majority of the world's oil and gas reserves,¹¹⁰ but they are also venturing out to invest internationally. For example, in 2002, China formally adopted a policy of encouraging its three main state-owned oil companies to engage in global exploration projects.¹¹¹ Moreover, with 84% of global growth in oil production over the next decade occurring in fifteen countries—only one of which, Canada, freely permits private exploration and development—the amount of reserves controlled by SOC's will only increase.¹¹²

The power of SOC's is not limited to oil companies such as Saudi Aramco, PdVSA, Pemex, National Iranian Oil Company, Kuwait Petroleum Company, Abu Dhabi National Oil Company, Nigerian National Petroleum Company, Gazprom, Rosneft, Chinese National Petroleum Company, Petrobras, and Statoil, to name a few. Indeed, SOC's are active market players in telecommunications, banking, and numerous other sectors.

While it is true that political or foreign policy reasons creep into (or in some cases, dominate) the commercial decisions of SOC's, for the most part such companies are market players in the same manner as their more traditional, non-state counterparts. SOC's participate in the international economy in a significant way, and they structure their holdings and investments much the same as traditional companies do. In order to demonstrate these characteristics of SOC's, it is helpful to consider three specific cases: (1) the Middle East (based upon a study of SOC's from five countries in the region); (2) Russia; and (3) Brazil. Fundamentally, while the bureaucratic nature and at times politically driven decision-making of SOC's distinguish them from their non-state counterparts, at

109. Rosenberg, *supra* note 2.

110. *Id.* Even in the 1970s, Western oil companies controlled over half of global oil production. They now produce only 13%, and the ten companies holding the world's largest reserves are all SOC's. Jad Mouawad, *As Oil Giants Lose Influence, Supply Drops*, N.Y. TIMES, Aug. 19, 2008, at A1(L).

111. Flynt Leverett & Pierre Noël, *The New Axis of Oil*, THE NATIONAL INTEREST, Summer 2006, at 66.

112. Patrice Hill, *State Monopolies Nudge Out Big Oil*, WASHINGTON TIMES, May 24, 2008, at A1. Indeed, Western oil companies "are being forced to renegotiate contracts on less-favorable terms and are fighting losing battles with assertive state-owned companies." Mouawad, *supra* note 110.

their core SOCs are commercial entities that interact with the marketplace much as traditional companies do.

1. The Middle East

Saudi Arabian oil production, resulting in more oil exports than any other country in the world,¹¹³ is spearheaded by the state-owned oil company, Saudi Aramco.¹¹⁴ Aramco has recently been initiating joint ventures with private investors in downstream activities in Saudi Arabia.¹¹⁵ Additionally, Aramco has interests in refineries in the United States, China, South Korea, Japan, and the Philippines.¹¹⁶ Its U.S. interests include three refineries in Louisiana and Texas that it holds jointly with Royal Dutch/Shell.¹¹⁷

Of course, Middle Eastern oil power is not limited to Saudi Arabia. A study conducted by Dr. Valérie Marcel (Principal Researcher with the Energy, Environment and Development Programme at Chatham House, home of the Royal Institute of International Affairs in London) from 2003 to 2005, involving numerous interviews with executives of the state oil companies of Saudi Arabia, Kuwait, Iran, Algeria, and Abu Dhabi, yielded much helpful information regarding how such SOCs function.¹¹⁸ Dr. Marcel found that these SOCs “want to operate like [international oil companies], though they are clearly national companies with public ownership of capital, special status in the hydrocarbon domain, obligations to the national market and a common history.”¹¹⁹ While these companies “wish to be seen as independent commercial entities . . . [they] play on their government’s relationship with the host country’s authorities to obtain deals.”¹²⁰

Dr. Marcel described the necessity for “clear distinction between the roles of each institution” (the SOC and its government owner):

Strategy is the plan of action by which the operator,

113. Energy Information Administration, U.S. Dep’t of Energy, Saudi Arabia Country Analysis Brief (Aug. 2008), http://www.eia.doe.gov/cabs/Saudi_Arabia/pdf.pdf.

114. Saudi Aramco has repeatedly been considered by courts to be an agency or instrumentality of a foreign state falling under the FSIA. *See, e.g.,* *Mendenhall v. Saudi Aramco*, 991 F. Supp. 856, 857-58 (S.D. Tex. 1998); *Good v. Aramco Servs. Co.*, 971 F. Supp. 254, 256 (S.D. Tex. 1997).

115. Saudi Arabia Country Analysis Brief, *supra* note 113.

116. *Id.*

117. *Id.*

118. MARCEL, *supra* note 3, at 10-12.

119. *Id.* at 55.

120. *Id.* at 71.

that is, the national oil company, the international oil company, or both set out how they will achieve the targets established by government. The potential blurring between the roles of government and [SOC] arises because the state is the shareholder of the company and, as such, participates in the strategy-making process. The state may indeed be represented on the supreme petroleum council (SPC), which approves the strategic plan, and on the company's board, which manages day-to-day operations. If the state is involved excessively in the management of operations, the national oil company's decisions will be relatively more influenced by political objectives, presumably to the detriment of commercial considerations.¹²¹

As described by a Saudi Aramco manager, “[w]e don’t set government policy (in relation to OPEC in particular). We make sure we don’t get sucked into their process. It’s better to divide these roles. We deliver the goods.”¹²² In Kuwait, on the other hand, Dr. Marcel found that “political interference hampers operations.”¹²³

Ultimately, Dr. Marcel concluded that “[SOCs] are now competing directly with [international oil companies] for projects and investment opportunities overseas, long the preserves of the supermajors.”¹²⁴ Moreover, “[i]n today’s high oil price environment, they have also been able to leverage their influence to an extent not seen in recent years.”¹²⁵ Finally, she noted, tellingly, that “[SOCs] are proving themselves able to compete head-on with [international oil companies] in everything from field development to mergers and acquisitions.”¹²⁶

2. Russia

Perhaps the most intriguing and politically complex example of how states utilize SOCs is presented by Russia. Gazprom and Rosneft, the largest Russian gas and oil companies respectively,¹²⁷ are

121. *Id.* at 77.

122. *Id.* at 80.

123. *Id.* at 85.

124. *Id.* at 228.

125. *Id.*

126. *Id.*

127. See Andrew E. Kramer, *As Gazprom Goes, So Goes Russia*, N.Y. TIMES, May 11, 2008, at 1 [hereinafter Kramer, *As Gazprom Goes*]; Rosneft History, <http://www.rosneft.com/printable/about/history> (last visited Mar. 4, 2009).

critical strategic parts of a newly assertive Russia. Indeed, that Russia's new President, Dmitri Medvedev, came to the presidency directly from his position as Gazprom chairman is not an insignificant fact.¹²⁸ These companies no doubt benefit significantly from their positions as Russia's favored sons; fully two-thirds of Rosneft's production comes from former Yukos property seized by the Russian authorities.¹²⁹ At the same time, their commercial policies tend to be aligned with the politically motivated directives of the Kremlin, as when Gazprom halted gas supplies to Ukraine following Ukraine's turn westward¹³⁰ or when Transneft (a Russian SOC that manages pipelines) slowed the flow of oil to the Czech Republic following that country's discussions with the United States regarding installation of missile defense radar detection equipment on Czech territory.¹³¹

Gazprom extracts more natural gas than any other company in the world.¹³² It also possesses the largest natural gas reserves and the largest gas transmission system in the world.¹³³ The Russian government holds a 50.002% interest in Gazprom,¹³⁴ whose stated goal is to "surpass Exxon Mobil as the world's largest publicly traded company" by 2014.¹³⁵

Rosneft, meanwhile, was created in 1993, inheriting assets once held by the USSR Ministry of Oil and Gas.¹³⁶ In 1995, Rosneft was opened to partial private ownership.¹³⁷ In recent years Rosneft has frequently acquired new oil assets within Russia—often owing to opportunities opened up by its parent, the Kremlin. In 2006, Rosneft engaged in a restructuring that involved the consolidation of twelve subsidiaries.¹³⁸ Additionally, it conducted a large IPO, placing approximately 15% of its shares in London and Moscow and raising about US\$10.7 billion.¹³⁹

As for Gazprom's international reach, much like a traditional multinational company, Gazprom owns numerous global assets,

128. Kramer, *As Gazprom Goes*, *supra* note 127.

129. Andrew E. Kramer, *Russia Fattens Up A State Oil Company*, N.Y. TIMES, June 8, 2006, at C7 [hereinafter Kramer, *Russia Fattens Up*].

130. *Id.*

131. Andrew E. Kramer, *Czechs See Oil Flow Fall and Suspect Russian Ire on Missile System*, N.Y. TIMES, July 12, 2008, at A5.

132. Kramer, *Russia Fattens Up*, *supra* note 129.

133. About/Gazprom Today, <http://www.gazprom.com/eng/articles/article8511.shtml> (last visited Mar. 4, 2009).

134. *Id.*

135. Kramer, *As Gazprom Goes*, *supra* note 128.

136. Rosneft History, <http://www.rosneft.com/printable/about/history> (last visited Mar. 4, 2009).

137. *Id.*

138. *Id.*

139. *Id.*

particularly gas distribution companies in Europe, including companies in Germany, the Czech Republic, Finland, Hungary, Italy, and the United Kingdom, among others.¹⁴⁰ Gazprom is also engaging in exploration and production in Venezuela, Libya, and Algeria.¹⁴¹ Finally, Gazprom is in the retail supply business in the United Kingdom, Denmark, France, Scandinavia, and Hungary, and also has a subsidiary in Houston that markets LNG and natural gas.¹⁴² In all, Gazprom has founded approximately sixty subsidiaries and also owns—wholly or in part—approximately 100 Russian or foreign companies.¹⁴³

While Gazprom enjoys numerous advantages due to its ownership by the Russian government, and its business decisions are at times driven by political policy, it functions much like a non-state company. Gazprom has a sophisticated corporate structure, is owned by international shareholders, has invested in various countries around the world, and enjoys numerous commercial relationships. Regardless of the source of its power, its activity is essentially commercial.

3. Brazil

Brazilian SOC Petrobras (the Brazilian government holds 55.7% of its voting shares) controls more than 95% of Brazil's crude oil production and is involved in all aspects of Brazil's oil sector.¹⁴⁴ Petrobras operates in twenty-three countries outside of Brazil. Included in its international operations are "interests in 331 offshore blocks in the United States" and a 50% interest in a Texas refinery.¹⁴⁵

Petrobras also owns a Cayman Islands company, Petrobras International Finance Company, that "acts as an intermediary between third-party oil suppliers and [Petrobras] by engaging in crude oil and oil product purchases from international suppliers, and reselling crude oil and oil products in U.S. dollars to [Petrobras]."¹⁴⁶ Petrobras has over two dozen direct and indirect subsidiaries.¹⁴⁷ Many of them are incorporated in Brazil, but several are

140. Nadejda Makarova Victor, *Gazprom: Gas Giant Under Strain* 26 (Stanford Program on Energy and Sustainable Dev., Working Paper No. 71, 2008).

141. *Id.* at 26-27.

142. *Id.* at 27.

143. *Id.*

144. Energy Information Administration, U.S. Dep't of Energy, Brazil Country Analysis Brief, (Sept. 2007), <http://www.eia.doe.gov/cabs/Brazil/pdf.pdf>.

145. Brazilian Petroleum Corp.-Petrobras. Annual report (Form 20-F), at 50, 52 (Dec. 31, 2007).

146. *Id.* at 53.

147. *Id.* Exhibit 8-1.

incorporated in the Cayman Islands, the Netherlands, the United Kingdom, Bermuda, and Singapore.¹⁴⁸

4. Trends from the Three Examples

Each of these examples involves companies whose essential purpose is commercial. There are, of course, several notable differences between these companies and traditional companies. For one, in the case of SOCs, dividends find their way into the national budget. To draw from a case discussed earlier, dividends from Pemex constitute approximately 40% of the Mexican national budget.¹⁴⁹ Additionally, as seen in particular with Gazprom and Rosneft, political considerations can often drive decision-making.

At their core, though, SOCs are fundamentally commercial. These companies engage in IPOs, have sophisticated corporate structures, invest in numerous ventures around the world, and otherwise engage in complex financial transactions. There is little justification for endowing these companies with such significant advantages over their non-state counterparts. The nature of these advantages is explored further in the following section.

D. The Current Exceptions to Immunity

As discussed above in Section I.A.2, the FSIA is based upon a system whereby certain entities enjoy a presumption of immunity. If the opposing party can demonstrate the existence of an applicable exception to immunity, the entity is not immune. Despite the availability of these exceptions, in many cases it is actually quite difficult for parties suing or attempting to attach the assets of an SOC to establish an applicable exception. As a result, the initial presumption of immunity is a significant advantage for SOCs.

First, and most importantly, the advantages with respect to immunity from execution enable an SOC to resist attachment or execution in a way that non-state companies cannot. Second, the commercial activity exception to immunity from jurisdiction can be difficult to establish. Finally, because courts are nervous to tackle issues that potentially impact U.S. foreign policy, the expropriation exception provides them with yet another way to avoid hearing cases addressing issues such as takings under international law.

148. *Id.*

149. *Running Just to Stand Still*, ECONOMIST, Dec. 19, 2007, at 55-56, available at http://www.economist.com/world/americas/displaystory.cfm?story_id=10328190.

1. Protection from Attachment

Section 1610 of the FSIA provides foreign states—including agencies and instrumentalities—with the tools to delay or hinder enforcement of judgments and to prevent the imposition of pre-judgment security.¹⁵⁰ Section 1610(a) lists the general exceptions to immunity from attachment or execution.¹⁵¹ Section 1610(b), meanwhile, provides a list of additional exceptions that apply to agencies and instrumentalities.¹⁵²

Critically, however, Section 1610(c) provides that

[n]o attachment or execution referred to in subsections (a) and (b) of this section shall be permitted until the court has ordered such attachment and execution after having determined that a reasonable period of time has elapsed following the entry of judgment and the giving of any notice required under section 1608(e) of this chapter.¹⁵³

While the FSIA does not specify what constitutes a reasonable period of time, in one case, the U.S. District Court for the Southern District of New York found thirty days to meet this standard.¹⁵⁴ This will often provide an SOC with ample time to move its assets after the issuance of a judgment against it. This grace period is, of course, not available to other market participants.

Additionally, Section 1610(d) provides an extremely high standard for the exception to immunity from pre-judgment attachment. Generally, SOCs are immune from pre-judgment attachment unless: (1) the property is used for commercial activity in the U.S.; (2) the SOC has *explicitly* waived its immunity from pre-judgment attachment; and (3) the purpose of attachment is to secure satisfaction of a judgment that has or may be entered, not to obtain jurisdiction.¹⁵⁵ While the third requirement is not difficult to establish, the first two requirements present significant obstacles to many efforts at pre-judgment attachment of the assets of an SOC.

With respect to the first requirement, that the property be used for commercial activity in the U.S., the term “commercial,” while not defined in the FSIA, refers to situations where the state acts as

150. 28 U.S.C. § 1610 (2000).

151. *Id.* § 1610(a).

152. *Id.* § 1610(b).

153. *Id.* § 1610(c).

154. *FG Hemisphere Assocs. v. Republique du Congo*, No. 01 CIV 8700SASHBP, 2005 WL 545218, at *7 (S.D.N.Y. Mar. 8, 2005) (order granting motion to execute on judgment).

155. 28 U.S.C. § 1610(d) (2000).

a private player in the market, rather than as a regulator.¹⁵⁶ In other words, an activity is commercial if it is the kind of activity in which private persons may engage, rather than the type of activity that is peculiar to a sovereign.¹⁵⁷ This amorphous standard has proven difficult, in many cases, for courts to apply.¹⁵⁸

Meanwhile, “commercial activity” is defined in Section 1603(d) of the FSIA as “either a regular course of commercial conduct or a particular commercial transaction or act. The commercial character of an activity shall be determined by reference to the nature of the course of conduct or particular transaction or act, rather than by reference to its purpose.”¹⁵⁹ It is important to note that the question of whether property is used for commercial activity in the U.S. has nothing to do with how the SOC generated the asset. Rather, the property must be “put into action, put into service, availed or employed *for* a commercial activity, not *in connection* with a commercial activity or *in relation* to a commercial activity” in the U.S.¹⁶⁰

SOCs may not have physical assets in the U.S., and savvy SOCs may not have cash sitting in a bank account in New York. Thus, a judgment debtor may find itself seeking intangible assets, such as receivables—the payment that a U.S. buyer owes to a state oil company for a purchase of crude, for example. Because “the situs of a debt obligation is the situs of the debtor,” such receivables are considered to be an asset located in the U.S.¹⁶¹ However, it is the rare case when an SOC has used such an asset for commercial activity in the U.S.; assigning the receivable or utilizing it as collateral for a loan are examples that come to mind.¹⁶²

Even if the judgment debtor can establish that the asset has

156. Republic of Arg. v. Weltover, Inc., 504 U.S. 607 (1992) (holding that bond issuance by the state is commercial); Tex. Trading & Milling Corp. v. Fed. Republic of Nigeria, 647 F.2d 300 (2d Cir. 1981) (holding that private contract to purchase goods is commercial).

157. Tex. Trading & Milling Corp., 647 F.2d at 309; see also De Sanchez v. Banco Central de Nicaragua, 770 F.2d 1385, 1392-93 (5th Cir. 1985) (holding that regulation and supervision of a nation's foreign exchange reserves is a sovereign activity); MOL, Inc. v. People's Republic of Bangladesh, 736 F.2d 1326, 1329 (9th Cir. 1984) (holding that only a state can regulate its imports and exports).

158. Joseph F. Morrissey, *Simplifying the Foreign Sovereign Immunities Act: If a Sovereign Acts Like a Private Party, Treat It Like One*, 5 CHI. J. INT'L L. 675, 684 (2005) (“[A]mbiguities and challenges exist for the courts in this regard. Fact patterns abound—[from expropriations to governmental trade in wildlife—]involving activities that do not easily lend themselves to characterizations as either private or governmental.”); Steven Swanson, *Jurisdictional Discovery Under the Foreign Sovereign Immunities Act*, 13 EMORY INT'L L. REV. 445, 455 (1999) (“Applying the [FSIA] has been far from simple. In particular, the commercial exception has proved to be troublesome.”).

159. 28 U.S.C. § 1603(d) (2000).

160. Af-Cap Inc. v. Chevron Overseas (Congo) Ltd., 475 F.3d 1080, 1091 (9th Cir. 2007).

161. Af-Cap Inc. v. Congo, 383 F.3d 361, 371 (5th Cir. 2004).

162. See *id.* at 363.

been used for commercial activity in the U.S., it also must show that the SOC has explicitly waived its immunity from pre-judgment attachment. A general waiver typically is insufficient, and a waiver of immunity from jurisdiction—or for that matter, a waiver of immunity from attachment—will not be construed as a waiver of immunity from pre-judgment attachment.¹⁶³ While the SOC need not use the phrase “prejudgment attachment” in order to constitute an explicit waiver,¹⁶⁴ establishing the presence of all three elements for the exception to immunity from pre-judgment attachment is a tall order indeed.

It is true that Section 1610(b) provides a lower standard for agencies and instrumentalities for post-judgment attachment—in particular, because the judgment debtor need not establish that the property itself has been used for commercial activity in the United States, but rather merely that the agency or instrumentality generally engages in commercial activity in the United States. However, it should be kept in mind that in such cases this showing must be coupled with a demonstration of an additional element.¹⁶⁵ In any event, the advantages accruing to SOCs from the “reasonable period of time” that must pass before a court can order execution, as well as the high barriers to pre-judgment attachment, tilt the playing field toward SOCs compared to their non-state counterparts.

2. The Commercial Activity Exception to Immunity from Jurisdiction

Plaintiffs are often not so fortunate as to have secured an explicit waiver from the foreign state of immunity from jurisdiction.

163. See, e.g., *O’Connell Mach. Co. v. M.V. “Americana”*, 734 F.2d 115, 117 (2d Cir. 1984) (finding that a waiver of “immunity ‘from suit, from execution of judgment, or from any other liability to which a privately owned and controlled enterprise is subject’ ” was not sufficient to establish a waiver of pre-judgment attachment).

164. *Banco de Seguros del Estado v. Mut. Marine Office, Inc.*, 344 F.3d 255, 258, 261 (2d Cir. 2003) (finding explicit waiver where arbitral agreements provided that the arbitrators “are relieved of all judicial formalities and may abstain from following the strict rules of law”); *Libra Bank Ltd. v. Banco Nacional de Costa Rica, S.A.*, 676 F.2d 47, 49 (2d Cir. 1982) (finding explicit waiver where the sovereign had agreed to “irrevocably and unconditionally waive[] any right or immunity from legal proceedings including suit judgment and execution on grounds of sovereignty which it or its property may now or hereafter enjoy”).

165. Specifically, the judgment debtor must demonstrate one of the following: (1) waiver of immunity from execution or attachment as stated in Section 1605(a)(1) (implicit or explicit, but simple waiver of immunity from jurisdiction is insufficient); (2) the action is based upon commercial activity as outlined in Section 1605(a)(2); (3) the action is based upon a taking in violation of international law pursuant to Section 1605(a)(3); (4) the action is based upon a case for money damages for personal injury or death or property damage as outlined in Section 1605(a)(5); or (5) the action is based upon a terrorist act as provided in Section 1605A.

In many cases, they simply have not had the opportunity. Moreover, the implicit waiver provision in Section 1605(a)(1) is construed very narrowly.¹⁶⁶ Thus, plaintiffs find themselves relegated to relying on another exception—most commonly the commercial activity exception.

Section 1605(a)(2) provides an exception to immunity from jurisdiction in any case

in which the action is based upon a commercial activity carried on in the United States by the foreign state; or upon an act performed in the United States in connection with a commercial activity of the foreign state elsewhere; or upon an act outside the territory of the United States in connection with a commercial activity of the foreign state elsewhere and that act causes a direct effect in the United States.¹⁶⁷

The definition of “commercial activity” and the types of activities that are “commercial” are discussed in Section III.D.1 above. Establishing that an SOC has engaged in commercial activity is straightforward; after all, most SOCs are inherently commercial. However, it is insufficient for the purposes of establishing an exception simply to demonstrate that the foreign state has engaged in commercial activity. Rather, the plaintiff must demonstrate a nexus between the foreign state’s commercial acts, the plaintiff’s claim, and the United States.¹⁶⁸

Section 1605(a)(2) provides three prongs under which this exception to immunity applies; in each case the claim is “based upon” a particular type of act. The court must focus on “those *specific* acts that form the basis of the suit.”¹⁶⁹ A claim is based upon those facts which, if proven, would entitle the “plaintiff to relief under his

166. See, e.g., *Shapiro v. Republic of Bol.*, 930 F.2d 1013, 1017 (2d Cir. 1991) (determining that the Republic of Bolivia did not implicitly waive sovereign immunity, even though it filed suit on associated claims in U.S. court); *Foremost-McKesson, Inc. v. Islamic Republic of Iran*, 905 F.2d 438, 444-45 (D.C. Cir. 1990) (refusing to find an implied waiver of sovereign immunity when the Republic of Iran failed to include a defense of sovereign immunity in its initial answer, and allowing Iran to file an amended answer with the defense). *But see Joseph v. Office of the Consulate Gen. of Nig.*, 830 F.2d 1018, 1022-23 (9th Cir. 1987) (holding that the waiver exception applied because the parties entered into a contract that specifically contemplated dispute resolution in U.S. courts but recognizing precedent for a narrow reading of implicit waiver).

167. 28 U.S.C. § 1605(a)(2) (2000).

168. *Vencedora Oceanica Navigacion v. Compagnie Nationale Algerienne de Navigation*, 730 F.2d 195, 200, 202 (5th Cir. 1984); *Sugarman v. Aeromexico, Inc.*, 626 F.2d 270, 272-73, 275 (3d Cir. 1980).

169. *Joseph v. Office of the Consulate Gen. of Nig.*, 830 F.2d 1018, 1023 (9th Cir. 1987) (emphasis in original).

theory of the case.”¹⁷⁰ As noted by the U.S. Court of Appeals for the Second Circuit, this suggests an extremely close connection between the act and the claim:

What does “based upon” mean? At a minimum, that language implies a causal relationship. . . . That is, it must be true that without the Act, there would be no judgments on which to sue. But this is not enough. . . . “[B]ased upon” requires a degree of closeness between the acts giving rise to the cause of action and those needed to establish jurisdiction that is *considerably greater than common law causation requirements*.¹⁷¹

Establishing the requisite nexus among the United States, the foreign state’s acts and the claims of the plaintiff is anything but straightforward as an evidentiary matter. As noted in the quote directly above, this nexus is “considerably greater” than what would apply in the context of a typical company.¹⁷² Thus, Section 1605(a)(2) is another example of how, due to the difficulty of establishing an applicable exception, the presumption of immunity is a significant advantage for SOCs.

The first prong under Section 1605(a)(2) applies where “the action is based upon a commercial activity carried on in the United States by the foreign state.”¹⁷³ According to Section 1603(e), “[a] ‘commercial activity carried on in the United States by a foreign state’ means commercial activity carried on by such state and having substantial contact with the United States.”¹⁷⁴

Saudi Arabia v. Nelson, decided by the U.S. Supreme Court in 1993, is the most prominent case addressing the first prong of Section 1605(a)(2).¹⁷⁵ Saudi Arabia, through its agent, had recruited Scott Nelson in the United States to work at a state-owned hospital in Saudi Arabia.¹⁷⁶ Following an interview in Saudi Arabia, Nelson signed an employment contract and attended an orientation session in the United States.¹⁷⁷ Several months after moving to Saudi Arabia, Nelson began complaining repeatedly about safety

170. *Saudi Arabia v. Nelson*, 507 U.S. 349, 357 (1993).

171. *Transatlantic Shiffahrtskontor GmbH v. Shanghai Foreign Trade Corp.*, 204 F.3d 384, 390 (2d Cir. 2000) (emphasis added).

172. *Joseph*, 204 F.3d at 390.

173. 28 U.S.C. § 1605(a)(2) (2000).

174. *Id.* § 1603(e).

175. *Saudi Arabia v. Nelson*, 507 U.S. 349, 351 (1993).

176. *Id.* at 352.

177. *Id.*

defects in the hospital's oxygen and nitrous lines.¹⁷⁸ Six months after his first complaints, Nelson was detained by Saudi agents, who brutally tortured him.¹⁷⁹ Nelson was then detained in a prison for over a month.¹⁸⁰ Eventually, following his return to the United States, Nelson filed suit against Saudi Arabia.¹⁸¹

While Saudi Arabia had recruited Nelson in the United States and Nelson had signed an employment contract and engaged in training in the United States, the Supreme Court found that Nelson's claim was not based upon those acts.¹⁸² Rather, his claim was based upon the alleged torts committed in Saudi Arabia, which were not commercial acts, let alone commercial acts committed in the United States.¹⁸³ Thus, the Court found that Saudi Arabia was immune from suit because Nelson had failed to establish that his suit was "based upon a commercial activity" carried on in the United States.¹⁸⁴ This case provides a clear example of the exacting manner in which courts demand that the specific acts at issue were commercial acts that occurred in the United States.¹⁸⁵

The second prong under Section 1605(a)(2) applies where "the action is based upon . . . an act performed in the United States in connection with a commercial activity of the foreign state elsewhere."¹⁸⁶ This seldom-applied prong "is 'generally understood to apply to non-commercial acts in the United States that relate to commercial acts abroad.'"¹⁸⁷ Of course, the claim must be based upon the act performed in the United States—not the commercial act abroad.¹⁸⁸

The final prong under Section 1605(a)(2) applies where "the action is based upon . . . an act outside the territory of the United States in connection with a commercial activity of the foreign state elsewhere and that act causes a direct effect in the United States."¹⁸⁹ That an American firm or individual suffers loss caused by a foreign act does not itself establish a "direct effect in the United States."¹⁹⁰ Indeed, the U.S. Court of Appeals for the Second Cir-

178. *Id.*

179. *Id.* at 352-53.

180. *Id.*

181. *Id.* at 353.

182. *Id.* at 358.

183. *Id.*

184. *Id.* at 358, 363.

185. *See id.*

186. 28 U.S.C. § 1605(a)(2) (2000).

187. *Byrd v. Corporacion Forestal y Industrial de Olancho S.A.*, 182 F.3d 380, 390 (5th Cir. 1999) (quoting *Voest-Alpine Trading USA Corp. v. Bank of China*, 142 F.3d 887, 892 n.5 (5th Cir.), *cert. denied* 119 S.Ct. 591 (1998)).

188. *Id.*

189. 28 U.S.C. § 1605(a)(2).

190. *Antares Aircraft, L.P. v. Fed. Republic of Nig.*, 999 F.2d 33, 36 (2d Cir. 1993).

cuit has stated that “[i]f a loss to an American individual and firm resulting from a foreign tort were sufficient standing alone to satisfy the direct effect requirement, the commercial activity exception would in large part eviscerate the FSIA’s provision of immunity for foreign states.”¹⁹¹

It is not necessary to establish that the effect be substantial or foreseeable.¹⁹² Rather, the effect must simply be direct—that is, an effect that follows “as an immediate consequence of the defendant’s . . . activity.”¹⁹³ Thus, the Supreme Court held that Argentina’s re-scheduling of bonds payable to accounts in New York—the place of performance for Argentina’s obligations—caused a direct effect in the United States.¹⁹⁴ The critical distinction in this case and others involving application of this prong is, according to the U.S. Court of Appeals for the Ninth Circuit, that “something legally significant actually happened in the U.S.”¹⁹⁵ Unlike the failure to fulfill a legal obligation within the United States, financial loss alone does not establish a direct effect.¹⁹⁶

In sum, the case law establishes what the U.S. Court of Appeals for the Fifth Circuit has stated succinctly: “The requirement under the FSIA of a connection between the plaintiff’s cause of action and the commercial acts of the foreign sovereign is a significant barrier to the exercise of subject-matter jurisdiction in United States courts.”¹⁹⁷

3. The Expropriation Exception

As courts tend to go out of their way to avoid hearing cases that relate to sovereigns, the FSIA provides them with a ready tool to dismiss such cases. The Act of State Doctrine and Political Question Doctrine provide ample opportunities for courts to avoid resolving cases that courts view as touching on sensitive international issues. In this respect, the FSIA has served as an additional means for courts to remove such disputes from their jurisdiction.

191. *Id.*

192. *Republic of Arg. v. Weltover, Inc.*, 504 U.S. 607, 617 (1992) (quoting *Weltover, Inc. v. Republic of Arg.*, 941 F.2d 145, 152 (2d Cir. 1991)).

193. *Id.* at 618 (alteration in the original) (quoting *Weltover, Inc. v. Republic of Arg.*, 941 F.2d 145, 152 (2d Cir. 1991)).

194. *Id.* at 618-19.

195. *Gregorian v. Izvestia*, 871 F.2d 1515, 1527 (9th Cir. 1989) (quoting *Zedan v. Kingdom of Saudi Arabia*, 849 F.2d 1511, 1515 (D.C. Cir. 1988)).

196. *Siderman de Blake v. Republic of Arg.*, 965 F.2d 699, 710 (9th Cir. 1992); *see also* *Alperin v. Vatican Bank, No. C-99-04941 MMC*, 2007 WL 4570674, at *7 (N.D. Cal. Dec. 27, 2007); *Adeler v. Fed. Republic of Nig.*, 107 F.3d 720, 726-27 (9th Cir. 1997).

197. *Stena Rederi AB v. Comision de Contratos del Comité Ejecutivo General*, 923 F.2d 380, 387 (5th Cir. 1991).

Cases decided under Section 1605(a)(3) provide a good example. As a reminder, this exception to jurisdictional immunity covers cases

in which rights in property taken in violation of international law are in issue and that property or any property exchanged for such property is present in the United States in connection with a commercial activity carried on in the United States by the foreign state; or that property or any property exchanged for such property is owned or operated by an agency or instrumentality of the foreign state and that agency or instrumentality is engaged in a commercial activity in the United States.¹⁹⁸

At the jurisdictional stage, the court does not need to decide whether the taking actually violated international law.¹⁹⁹ Rather, as long as a claim is substantial and non-frivolous, this requirement is met.²⁰⁰ Nonetheless, in 37 of 47 cases found by the author in which Section 1605(a)(3) was at issue, the plaintiff's claim was dismissed relatively quickly because the plaintiff could not establish the applicability of the exception.²⁰¹

Nemariam v. Federal Democratic Republic of Ethiopia,²⁰² decided by the U.S. Court of Appeals for the D.C. Circuit in 2007, is a good example of the lengths to which courts will go to avoid hearing such cases. The plaintiffs, individuals of Eritrean origin who had been expelled from Ethiopia during the armed conflict between Eritrea and Ethiopia, claimed that the Central Bank of Ethiopia ("CBE") had prevented them from accessing their bank accounts.²⁰³ While the court found that intangible property such as bank accounts (a right to receive payment from a bank) can fall

198. 28 U.S.C. § 1605(a)(3) (2000).

199. *Siderman de Blake*, 965 F.2d at 711.

200. *Id.*

201. Eleven of these cases were decided at the Circuit Court of Appeals level. See *Nemariam v. Fed. Democratic Republic of Eth.*, 491 F.3d 470 (D.C. Cir. 2007); *Garb v. Republic of Pol.*, 440 F.3d 579 (2d Cir. 2006); *Peterson v. Royal Kingdom of Saudi Arabia*, 416 F.3d 83 (D.C. Cir. 2005); *Zappia Middle East Construction Co. Ltd. v. Emirate of Abu Dhabi*, 215 F.3d 247 (2d Cir. 2000); *Gabay v. Mostazafan Found. of Iran*, No. 97-7826, 1998 WL 385909 (2d Cir. May 4, 1998); *Antares Aircraft, L.P. v. Federal Republic of Nigeria*, 948 F.2d 90 (2d Cir. 1991); *Chuidian v. Philippine Nat'l Bank*, 912 F.2d 1095 (9th Cir. 1990); *Brewer v. Socialist People's Republic of Iraq*, 890 F.2d 97 (8th Cir. 1989); *Dayton v. Czechoslovak Socialist Republic*, 834 F.2d 203 (D.C. Cir. 1987); *De Sanchez v. Banco Central de Nicar.*, 770 F.2d 1385 (5th Cir. 1985); *Vencedora Oceanica Navigacion, S.A. v. Compagnie Nationale Algerienne de Navigation*, 730 F.2d 195 (5th Cir. 1984).

202. 491 F.3d 470 (D.C. Cir. 2007).

203. *Id.* at 472-73.

within the Section 1605(a)(3) exception—even if they remain outside of the Second Hickenlooper Amendment that prevents application of the Act of State Doctrine to such cases involving tangible property²⁰⁴—the resolution of the case came down to application of the Section 1605(a)(3) requirement that the agency or instrumentality “owned or operated” such property.²⁰⁵ The court dismissed the plaintiffs’ claims on the following grounds:

[t]he CBE owns the funds in the appellants’ accounts. The *property right* at issue, however, is the appellants’ *contractual right to receive payment* and the CBE has neither taken possession of nor exerted control over that right. Instead, accepting as true the appellants’ allegation that Ethiopia and the CBE have in fact prevented them from accessing the funds in the accounts, . . . we believe the CBE has *extinguished* that contract right. . . . That is, the CBE did not assume the appellants’ contractual right to performance[—]instead it declined to perform its own contractual obligations.²⁰⁶

This case is merely one example, but the FSIA serves to provide courts with an easy way out because it involves what courts do best: step-by-step application of the particular language of a statute. If a court can apply the nuanced wording of a statute to avoid hearing a case, rather than applying the “fuzzier” standards related to the Act of State or Political Question Doctrines, then it will seize that opportunity.²⁰⁷

204. The Second Hickenlooper Amendment provided that unless (1) the act of the foreign state is not contrary to international law or (2) the President instructs the court otherwise, no court shall decline on the grounds of the act of state doctrine to hear a claim on the merits for a case “in which a claim of title or other right to property is asserted by any party including a foreign state . . . based upon (or traced through) a confiscation or other taking after January 1, 1959.” 22 U.S.C. § 2370(e)(2) (2000). The courts have generally interpreted the Second Hickenlooper Amendment to apply to confiscations of tangible property only. See, e.g., *Menendez v. Saks & Co.*, 485 F.2d 1355 (2d Cir. 1973) *rev’d in part on other grounds sub nom.* *Alfred Dunhill of London, Inc. v. Republic of Cuba*, 425 U.S. 682 (1976); *Canadian Overseas Ores, Ltd. v. Compania de Acero del Pacifico S.A.*, 528 F. Supp. 1337, 1346 (S.D.N.Y. 1982).

205. *Nemariam*, 491 F.3d at 479-80.

206. *Id.* at 481 (citations omitted).

207. Admittedly, under the particular facts of *Nemariam*, CBE as a central bank would indeed constitute a “foreign state” under the revised definition proposed in this Article. The point, however, relates to the interpretation of the statute, which would also have applied if the plaintiffs had been owed money—or oil—by an SOC.

IV. A PROPOSED FRAMEWORK

As discussed above, the body of cases applying Section 1603(b) has been anything but a model of clarity, sowing much confusion and unpredictability both for sovereigns and for those interacting with sovereigns' subsidiaries in the market. Paradoxically, many such subsidiaries benefit from immunity while their owners benefit from separate corporate status. The enormous commercial influence exerted by SOCs suggests that they should be treated the same as any traditional, non-state company. All of these factors point to one conclusion: SOCs should not be entitled to any presumption of immunity at all.

Implementing such a principle could be done only by amending the FSIA. This amendment would not be simply a matter of eliminating agencies and instrumentalities from the scope of the FSIA, however, as many government entities that should enjoy immunity—departments, ministries and central banks—could fit within the current definition of agencies and instrumentalities.²⁰⁸ Thus, the definition of “foreign state” more generally would need to be tweaked to provide that certain types of governmental entities are entitled to a presumption of immunity, irrespective of their ability to sue or be sued or enter into contracts in their own name.

A. Proposed Amendments to the FSIA

Section 1603 of the FSIA should be amended to read as follows:

- (a) A “foreign state” includes the following:
 - (1) the central government and its embassies, consulates and other diplomatic facilities abroad;
 - (2) all political subdivisions, including states, provinces, cities and other regional and local subdivisions;
 - (3) all state entities, agencies and offices whose principal, fundamental purpose and activity is public, rather than commercial, in nature, including departments, ministries, the armed services, regulatory agencies and other such entities, agencies and offices of the central government and its political subdivisions; and
 - (4) the central bank of that foreign state.

208. See H.R. REP. NO. 94-1487, at 15-16 (1976), as reprinted in U.S.C.C.A.N. 6604, 6614.

Section 1603(b), which provides the definition for “agency or instrumentality of a foreign state,” would be deleted. This amendment would also require corresponding amendments in Sections 1605, 1606 (punitive damages), 1608 (service) and 1610 to eliminate references to agencies and instrumentalities.

Amending Section 1603 in this manner would provide greater predictability by specifying in more precise detail the entities that are considered to be part of the foreign state. These amendments would also ensure that only those government entities whose purpose and activity is essentially public would enjoy a presumption of immunity. Meanwhile, SOCs—whose purpose and activity are typically commercial in nature—would enjoy no presumption of immunity. Following such amendments, the law would treat SOCs as it would any other company with respect to jurisdiction; it would depend upon the typical standards of due process, minimum contacts²⁰⁹ and long-arm statutes.²¹⁰

While these changes would alter the legal landscape significantly, they would do so in a manner consistent with principles long applied by U.S. courts. As noted by the United States Court of Appeals for the Eighth Circuit:

From the earliest days of our Republic, courts have distinguished between the public and private acts of government. Public acts, such as punishing criminals and printing money, emanate from the power inherent in sovereignty. Private acts, such as commercial transactions, are not unique to government and could be performed by an individual. Jurisdictional consequences flow from this distinction between public and private acts.²¹¹

These principles underlie the restrictive theory of sovereign immunity, which Congress intended to implement into U.S. law through the FSIA.²¹² If SOCs continue to enjoy a presumption of immunity, these principles are applied superficially at best. It is

209. See *World-Wide Volkswagen Corp. v. Woodson*, 444 U.S. 286, 291 (1980) (noting that “[a] state court may exercise personal jurisdiction over a nonresident defendant only so long as there exist ‘minimum contacts’ between the defendant and the forum State”).

210. See *Burger King Corp. v. Rudzewicz*, 471 U.S. 462, 464, 487 (1985) (holding that Florida’s long-arm statute did not offend traditional conceptions of fair play and justice embodied in the Due Process Clause of the Fourteenth Amendment and, therefore, the statute gave rise to jurisdiction in U.S. District Court in Florida).

211. *BP Chems. Ltd. v. Jiangsu Sopo Corp.*, 285 F.3d 677, 681 (8th Cir. 2002) (internal citations omitted).

212. See H.R. REP. NO. 9401487, at 9-6.

only through amendment of the FSIA that they will be carried out in practice.

Finally, it is important to note that these changes would not revamp the FSIA entirely. In fact, the basic structure—in which a foreign state is presumed immune unless the plaintiff can establish that an exception to immunity applies—would remain in place. For the most part, the FSIA has been an enormous success in an area that badly needed codification. The problem outlined in this Article—and intended to be addressed by the amendments proposed above—is that this structure has been applied to certain entities that should fall outside the immunity regime applicable to foreign states. The structure should remain in place—minus SOCs.

Of course, it is rarely easy to amend a statute, particularly one that has been in place for some time. However, Congress has shown that it can amend the FSIA when it needs to do so. Congress amended the FSIA in 1996 and in 2007, in each case to allow victims of terrorism to seek compensation from foreign states.²¹³ The amendments proposed in this Article are very narrow and targeted, focused on a particular issue. The problems outlined above are extensive, but there is a relatively simple, straightforward solution.

B. *The 2002 ABA Working Group Report*

The author is not the only one who has been considering how to revise the FSIA. In 2002, a working group of the American Bar Association issued a report (the “ABA Report”) entitled “Reforming the Foreign Sovereign Immunities Act.”²¹⁴

The ABA Report noted initially that “[o]ver the course of the past twenty-five years, judicial interpretations of the statute have highlighted some of the shortcomings, ambiguities, and problems of the [FSIA]. Although courts have resolved certain of these problems, many remain, some of which are not easily addressed by the

213. In 1996, Congress passed the Antiterrorism and Effective Death Penalty Act, which amended Section 1605 of the FSIA by creating a new exception that would apply when terrorism victims sued individuals employed by foreign sovereigns for engaging in or supporting various acts of terrorism. Antiterrorism and Effective Death Penalty Act of 1996, Pub. L. No. 104-132, § 221, 110 Stat. 1214, 1241-42 (to be codified at 28 U.S.C. § 1605). In the same year, Congress also passed the “Flatow Amendment” to the FSIA, which permitted punitive damages for state-sponsored terrorism. Foreign Operations, Export Financing, and Related Programs Appropriations Act, 1997 Pub. L. No. 104-208, § 589, 110 Stat. 3009, 3009-172 (to be codified at 28 U.S.C. § 1605). In 2008, Congress again amended Section 1605, further enhancing the ability of individuals to sue states for acts of terrorism. National Defense Authorization Act for Fiscal Year 2008, Pub. L. No. 110-181, § 1083, 122 Stat. 337, 338-44 (to be codified at 28 U.S.C. § 1605A).

214. Working Group of the Am. Bar Ass’n, *supra* note 59.

courts.”²¹⁵ The ABA Report set out to address such issues—including, among others, “the scope of the term ‘foreign state’”²¹⁶—by proposing amendments to the FSIA. The ABA Report was thoroughly researched, and much of its discussion is relevant to the issues discussed in this Article. Some of its proposals, however, did not go far enough and would leave in place a statute that applies, inappropriately, to SOCs.

Two proposals of the ABA Report are worth discussing in the context of this Article: (1) adoption of the “legal characteristics” test rather than the “core function” test for the purposes of distinguishing between foreign states proper and agencies/instrumentalities;²¹⁷ and (2) extension of the “majority ownership” prong to entities held indirectly by the foreign state.²¹⁸

The ABA Report found that in distinguishing between foreign states proper and agencies/instrumentalities, “the legal characteristics test is the more appropriate test.”²¹⁹ Appropriate factors for consideration would “include whether the entity maintains a distinct personality, was sufficiently capitalized, observes corporate formalities, maintains corporate records, holds property in its own name, contracts in its own name, and is able to sue and be sued.”²²⁰ However, the ABA Report also recognized that although “some governments give contract and litigation powers to certain entities . . . this does not mean that the entity operates independently of the state. Government departments, ministries, and regulatory agencies can be in this position.”²²¹ Thus, the ABA Report proposed modifying the definition of “foreign state” to clarify that the state includes “departments and ministries of government,” as well as “the armed services and independent regulatory agencies.”²²²

This proposal is sensible, and it has been incorporated into the amendments proposed in this Article. In fact, while the ABA Report claimed to have adopted the legal characteristics test,²²³ the above-mentioned carve-outs actually provide for a hybrid test. It is not the case that one test is objectively better than the other; rather, both are valid and relevant. It is a matter of striking the appropriate balance so that the entities that intuitively should be entitled to presumptive immunity are in fact provided with this pre-

215. *Id.* at 489.

216. *Id.*

217. *Id.* at 514-16.

218. *Id.* at 522-27.

219. *Id.* at 514.

220. *Id.* at 515.

221. *Id.*

222. *Id.*

223. *Id.* at 514-16.

sumption, and that those that are not so entitled do not unjustly enjoy this benefit. Where the ABA Report fell short, however, was in keeping in place the application of the FSIA to instrumentalities such as SOCs.²²⁴

Second, the ABA Report proposed that presumptive immunity be extended to indirect subsidiaries of foreign states.²²⁵ Of course, following the Supreme Court's decision in *Dole Food Co. v. Patrickson*,²²⁶ such a proposal necessitates legislative action, rather than merely a choice between conflicting court interpretations. However, in an age when foreign states structure their subsidiaries in a sophisticated manner, the majority ownership prong is an entirely inadequate test—whether it be merely one option or the exclusive means to establish agency/instrumentality status.

The number of tiers between a foreign state and an SOC has little to do with the control that that foreign state exercises over the SOC or otherwise with its “sovereignness.” The intervening tiers could be merely inactive holding companies, for example. Or, for that matter, a foreign state in theory could manipulate its holding structure so that it holds all of its subsidiaries directly, in one tier. Of course, the foreign state's control over and involvement in the operations of each company, as well as the public or commercial nature of each company, could vary dramatically. All in all, whether an SOC is held directly is more a matter of form than substance. In any event, Congress should be eliminating the application of the FSIA to SOCs, not expanding its scope.

C. *Potential Impact of the Proposed Changes on the International Legal Landscape*

Sovereign immunity is derived from international law. In practice, however, principles of sovereign immunity are most typically applied in jurisdictions around the world at the level of national legal systems. The development of the law governing sovereign immunity has thus occurred mostly at the national level. Rather than being hashed out at an international conference or in international courts, the legal principles applying to sovereign immunity have been developed by individual jurisdictions.

At times, these jurisdictions may be influenced by the development of the law in foreign jurisdictions. As the U.S. Congress considered enactment of the FSIA in 1976, for example, the House

224. *Id.* at 508.

225. *Id.* at 522-23.

226. 538 U.S. 468 (2003).

Report noted that the FSIA “[was] also designed to bring U.S. practice into conformity with that of most other nations by leaving sovereign immunity decisions exclusively to the courts.”²²⁷ If the United States was following other nations in 1976, it now has an opportunity to modernize the FSIA in a way that can serve as a model for other nations. The proposed changes are intuitive in the current climate, and they will not go unnoticed abroad.

While development of the principles of sovereign immunity at the international level has not been completely absent, it has not gone very far. On December 2, 2004, the United Nations General Assembly adopted the *United Nations Convention on Jurisdictional Immunities of States and Their Property* (the “UN Convention”).²²⁸ The UN Convention would enter into force only once thirty states had deposited original instruments of ratification, acceptance, approval or accession.²²⁹ While the UN Convention was open for signature from January 17, 2005 until January 17, 2007, only twenty-eight states signed the Convention during that period.²³⁰ As of January 2009, only six states had deposited instruments of ratification.²³¹ The United States has not signed the UN Convention.²³²

With respect to the Convention’s rationale, the Preamble provides that the Convention “would enhance the rule of law and legal certainty, particularly in dealings of States with natural or juridical persons, and would contribute to the codification and development of international law and the harmonization of practice in this area.”²³³ The UN Convention offers the following definition of the term “State”:

- (i) the State and its various organs of government;
- (ii) constituent units of a federal State or political subdivisions of the State, which are entitled to perform acts in the exercise of sovereign authority, and are acting in that capacity;
- (iii) agencies or instrumentalities of the State or other entities, to the extent that they are entitled to perform and are actually performing acts in the exercise

227. H.R. REP. NO. 94-1487, at 12 (1976), *as reprinted in* 1976 U.S.C.C.A.N. 6604, 6610.

228. G.A. Res. 59/38, ¶ 3, U.N. Doc. A/RES/59/38 (Dec. 2, 2004).

229. United Nations Convention on Jurisdictional Immunities of States and Their Property art. 30(1), *adopted* Dec. 2, 2004, 44 I.L.M. 803, 812.

230. Status of United Nations Convention on Jurisdictional Immunities of States and Their Property, <http://treaties.un.org/Pages/ViewDetails.aspx?src=UNTSO&tabid=2&id=284&chapter=3&lang=en> (last visited Mar. 4, 2009).

231. *Id.*

232. *See id.*

233. United Nations Convention on Jurisdictional Immunities of States and Their Property, *supra* note 229, pmb1.

of sovereign authority of the State;
(iv) representatives of the State acting in that capacity.²³⁴

The vagueness of subsection (iii) of the proposed definition of “State” is problematic. It is unclear when an entity is “performing acts in the exercise of sovereign authority of the State.” Moreover, it appears that no particular connection to the State is necessary for the entity, other than its qualifying as an agency or instrumentality—terms left undefined—and being “entitled to perform” such acts.

Regardless of the failure of the UN Convention to address the concerns at the heart of this Article, an insufficient number of states has signed or ratified the Convention. Efforts at the international level to develop the legal principles governing sovereign immunity have been unsuccessful, so these principles will continue to be developed mainly at the domestic level. As recently noted by Professor Catherine Powell of Fordham Law School in the human rights context:

Because international law is “incomplete,” it is interpretatively open and invites domestic actors to be involved in the process of its creation. In the U.S. context, this means that norms developed democratically at the domestic level play a gap-filling function and have the potential to inform international law (and vice versa) through a continually iterative process.²³⁵

Similarly, norms developed at the domestic level can also inform international legal principles—such as those governing sovereign immunity—embedded in other domestic legal systems. Thus, modernization of the FSIA by the United States could potentially have an impact on the modernization of sovereign immunity globally.

CONCLUSION

We live in an era of increasingly powerful and influential SOCs. The current legal regime provided by the FSIA, as interpreted by the courts, is not only outdated in its application to SOCs, it is also conflicting and confusing. The best way to solve this problem is to amend the FSIA so that SOCs no longer enjoy a

234. *Id.* art. 2(1)(b).

235. Catherine Powell, *Tinkering with Torture in the Aftermath of Hamdan: Testing the Relationship Between Internationalism and Constitutionalism*, 40 N.Y.U. J. INT'L L. & POL. 723, 738 (2008) (footnote omitted).

presumption of immunity. Doing so will better honor the restrictive theory of sovereign immunity applied around the world, including the United States since 1952.

No legislation is perfect. Times change, and it is only following the development of case law over a period of decades that the myriad implications of a statute become clear. Implementation of the amendments proposed in this Article would provide a clear, predictable legal framework for SOCs that will provide stability both for sovereigns and for the companies with whom sovereigns and their subsidiaries do business.

