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The All New (International) People's Court: The Future of the Direct Effect Clause after Voest-Apline Trading USA Corp v. Bank of China

Matthew Bensen

Comment

The All New (International) "People's Court": The Future of the Direct Effect Clause After *Voest-Alpine Trading USA Corp. v. Bank of China*

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Over the past ten years, economic reform in former communist and developing countries has stimulated significant change and expansion in the global marketplace. In an effort to encourage foreign investment, developing countries have increasingly entered the market as private parties engaging in commercial transactions.[1] Foreign governments now play a prominent role in international finance, investment, and trade in industries such as shipping, agriculture, banking transactions, and oil production.[2] While this participation has created more international opportunities for American business, the benefits have not come without consequence. Greater interaction with foreign governments has increased the potential for international commercial disputes.[3] These disputes raise the question of when U.S. courts can exercise jurisdiction over foreign sovereigns participating in international commercial transactions.

The Fifth Circuit recently dealt with this issue in *Voest-Alpine Trading USA Corp. v. Bank of China*.[4] At issue in the case was an agreement between Voest-Alpine, an American corporation, and the Jiangyin Foreign Trade Corporation (JFTC), a

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1. *See* Michael D. Ramsey, *Acts of State and Foreign Sovereign Obligations*, 39 HARV. INT'L L.J. 1, 1 (1998); *see also* Cicippio v. Islamic Republic of Iran, 30 F.3d 164, 167 (D.C. Cir. 1994).

2. *See* JOHN R. STEVENSON ET AL., UNITED STATES LAW OF SOVEREIGN IMMUNITY RELATING TO INTERNATIONAL FINANCIAL TRANSACTIONS 1-3 (1983).

3. *See* Richard Wydeven, *The Foreign Sovereign Immunities Act of 1976: A Contemporary Look at Jurisdiction Under the Commercial Activity Exception*, 13 REV. LITIG. 143, 143 (1993).

4. 142 F.3d 887 (5th Cir. 1998), *cert. denied*, 119 S. Ct. 591 (1998).

company based in China, for the overseas delivery of roughly one million dollars worth of styrene monomer.[5] The Bank of China, a government instrumentality, provided security for JFTC's payment obligation by issuing an irrevocable letter of credit in the amount of 1.2 million dollars.[6] After performing its part of the agreement, Voest-Alpine contacted the Bank of China requesting payment,[7] but was told in response that JFTC had refused to issue payment.[8]

Voest-Alpine subsequently brought an action against the Bank of China seeking damages for breach of the letter of credit.[9] The Bank of China moved to dismiss for lack of jurisdiction and improper venue, asserting its immunity under the Foreign Sovereign Immunities Act (FSIA).[10] Citing several circuit court decisions, the Bank of China maintained that it was entitled to immunity because it had not engaged in any "legally significant act" in the United States.[11] The Fifth Circuit rejected this argument, holding that a financial loss incurred in the United States by an American plaintiff supports jurisdiction over a foreign government if it is an "immediate consequence" of the defendant's activity.[12]

The decision in *Voest-Alpine* departs significantly from recent interpretations of the FSIA. Circuit courts have generally interpreted the Act as imposing a requirement that a foreign sovereign participating in commercial transactions outside the United States commit some "legally significant act" in the United States before being subjected to jurisdiction.[13] In contrast, the court in *Voest-Alpine* expressly rejected the legally significant act requirement, opting instead for a lower standard that favors jurisdiction over sovereign immunity.[14] This preference for jurisdiction may ultimately cause foreign gov-

5. *See id.* at 890.

6. *See id.*

7. *See id.* Voest-Alpine sought to collect on the irrevocable letter of credit as payment for the delivery. *See id.*

8. *See id.* It is not entirely clear why JFTC refused to pay, but they claimed that there were discrepancies in the documents for presentment to the Bank of China.

9. *See id.* at 890-91.

10. 28 U.S.C. §§ 1330, 1602-1611 (1994).

11. *See Voest-Alpine*, 142 F.3d at 894.

12. *See id.* at 897.

13. *See* discussion *infra* Part I.E.

14. *See Voest-Alpine*, 142 F.3d at 894-95.

ernments to avoid transactions with American businesses, thereby affecting the stability of the international market.[15]

This Comment argues that the Fifth Circuit erred in rejecting the legally significant act requirement. Part I discusses the history of sovereign immunity in the United States, the development of the FSIA, and subsequent interpretations of the commercial activities exception. Part II discusses the Fifth Circuit's holding and reasoning in *Voest-Alpine*. Part III argues that the court improperly rejected the legally significant act requirement and outlines the problems associated with extending the jurisdictional reach of U.S. courts. Finally, this Comment concludes that the standard articulated in *Voest-Alpine* is insufficient to ensure stability in foreign markets. The legally significant act requirement provides a better solution because it represents a fair compromise between protecting American business and respecting foreign sovereignty.

I. THE ROAD TO THE MODERN COMMERCIAL ACTIVITY EXCEPTION

A. THE THEORY OF ABSOLUTE IMMUNITY AND ITS DEVELOPMENT IN UNITED STATES COURTS

The traditional concept of sovereign immunity held that domestic courts should refrain from exercising jurisdiction over a foreign state.[16] The historical basis for granting immunity was reflected in the old maxim *rex non potest peccare*,[17] which suggested that sovereign equals have no dominion over each other.[18] In more recent times, the doctrine of sovereign immunity has been supported by the view that it is necessary to respect the independence, equality, and dignity of foreign states.[19]

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15. *See* Stephen J. Leacock, *The Joy of Access to the Zone of Inhibition:* Republic of Argentina v. Weltover, Inc. *and the Commercial Activity Exception Under the Foreign Sovereign Immunities Act of 1976*, 5 MINN. J. GLOBAL TRADE 81, 121 (1996).

16. *See* William R. Dorsey, III, *Reflections on the Foreign Sovereign Immunities Act After Twenty Years*, 28 J. MAR. L. & COM. 257, 257 (1997).

17. The phrase *rex non potest peccare* is Latin for "the King can do no wrong." BLACK'S LAW DICTIONARY 1323 (6th ed. 1990).

18. *See* Leacock, *supra* note 15, at 85.

19. *See* MICHAEL WALLACE GORDON, FOREIGN STATE IMMUNITY IN COMMERCIAL TRANSACTIONS 1-2 (1991).

United States courts first recognized sovereign immunity in 1812 in *The Schooner Exchange v. McFaddon*.[20] Although the Court intended its holding to be fact-specific, courts and commentators have generally agreed that *The Schooner Exchange* established the doctrine of absolute immunity for foreign sovereigns in U.S. courts.[21] Domestic courts could not exercise jurisdiction over foreign states irrespective of whether they were engaged in governmental or commercial acts.[22]

B. THE SHIFT TO A RESTRICTIVE THEORY OF IMMUNITY

The amount of protection afforded to foreign sovereigns under the doctrine of absolute immunity was "increasingly criticized . . . throughout the first half of the twentieth century."[23] As foreign states engaged in more commercial activi-

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20. 11 U.S. (7 Cranch) 116 (1812). *The Schooner Exchange* involved a libel and arrest claim made by United States plaintiffs against a French warship. *Id.* at 117. The plaintiffs claimed that they had operated the vessel privately, and that it left the U.S. en route to Spain. *See id.* Months later, Napoleon's army seized the ship and converted it into a military vessel. *See id.* The ship later sailed into United States waters near Philadelphia, where the plaintiffs brought suit. *See id.* The Supreme Court held the vessel to be immune from suit, relying on a theory of absolute sovereign immunity. *See id.* at 146-47; *see also* Verlinden B.V. v. Central Bank of Nigeria, 461 U.S. 480, 486 (1983) (discussing the decision in *The Schooner Exchange*).

21. *See Verlinden*, 461 U.S. at 486 ("[The] opinion came to be regarded as extending virtually absolute immunity to foreign sovereigns."); *see also* David E. Gohlke, *Clearing the Air or Muddying the Waters? Defining "A Direct Effect in the United States" Under the Foreign Sovereign Immunities Act After* Republic of Argentina v. Weltover, 18 HOUS. J. INT'L L. 261, 265 (1995) (noting that application of absolute immunity is generally traced to *The Schooner Exchange*). There is some indication in the opinion, however, that the Court might have accepted a restrictive theory even at this early date. The Court noted that "a prince, by acquiring private property in a foreign country . . . may be considered [to be] laying down the prince, and assuming the character of a private individual." 11 U.S. (7 Cranch) at 145. The restrictive theory surfaced again in a later case, where the Court suggested that when a government actively participates as a partner in a commercial venture, it divests itself of its sovereign character, and takes on that of a private citizen. *See* Bank of the United States v. Planters' Bank of Georgia, 22 U.S. (9 Wheat.) 904, 907 (1824).

22. *See* Dorsey, *supra* note 16, at 258.

23. Joan E. Donoghue, *Taking the "Sovereign" out of the Foreign Sovereign Immunities Act: A Functional Approach to the Commercial Activity Exception*, 17 YALE J. INT'L L. 489, 496 (1992); *see id.* at 496 n.31 (listing commentators who criticized absolute immunity). Donoghue also notes that "[t]he notion of absolute sovereignty . . . declined in importance, and by the end of the Second World War commentators generally agreed that state sovereignty was a relative notion limited by the sovereignty of other states." *Id.* at 496-97 (citations omitted). The initial decline in the notion of absolute sovereignty

ties that resulted in commercial disputes, the potential for non-U.S. sovereigns to abuse sovereign immunity had increased.[24] This prompted the State Department in 1952 to alter its position on the question of immunity and release the "Tate letter" announcing the adoption of a restrictive theory of sovereign immunity.[25] Under the restrictive theory, sovereign immunity is limited to a foreign government's public acts (*jure imperii*) and does not extend to suits involving its commercial or private acts (*jure gestionis*).[26]

Adoption of the restrictive theory, however, did not eliminate concerns over the possible abuse of sovereign immunity.[27] Diplomatic pressure and political considerations often led the

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began in Europe at the 1926 Brussels Convention for the Unification of Certain Rules Relating to the Immunity of State-Owned Vessels. *See* GORDON, *supra* note 19, at 1-4. This convention established immunity rules equating publicly-owned merchant vessels with those privately-owned, which meant that immunity would be denied to foreign states when they operated state-owned merchant vessels. *See id.* Twenty nations signed the Convention in 1926, but the United States did not participate. *See id.*

24. *See* Avi Lew, Republic of Argentina v. Weltover, Inc.: *Interpreting the Foreign Sovereign Immunity Act's Commercial Activity Exception to Jurisdictional Immunity*, 17 FORDHAM INT'L L.J. 726, 731-32 (1994) ("As sovereigns increased their participation in the world market, there was an increase in the possibility that nations could invoke the sovereign immunity defense. . . . Therefore, the potential for non-U.S. sovereigns to abuse sovereign immunity had increased."); *see also* STEVENSON ET AL., *supra* note 2, at 1-3 (explaining that foreign governments not only engaged in a substantial amount of borrowing, but also participated more directly and frequently in many forms of international trade and transactions). This increased participation led to the need for more stability in international contracts. *See id.* at 2-3. Persistent strains on the economies of certain countries increased the possibility that foreign governments could default on their commercial obligations. *See id.* As a result, parties involved in transactions with sovereign entities sought adequate legal safeguards to ensure that commercial disputes were properly adjudicated. *See id.*

25. *See* JOSEPH W. DELLAPENNA, SUING FOREIGN GOVERNMENTS AND THEIR CORPORATIONS 7 (1988). The Tate letter noted that most countries that had previously supported the classical theory had ratified the Brussels Convention of 1926. *See* Letter from Jack B. Tate, Acting Legal Adviser, Department of State, to Acting Attorney General Philip B. Perlman (May 19, 1952), *reprinted in* 26 DEP'T ST. BULL. 984-85 (1952), *and in* Alfred Dunhill, Inc. v. Republic of Cuba, 425 U.S. 682, 711-15 (1976) (app. 2 to opinion of White, J.) [hereinafter Tate Letter]. Recognizing that there was little support remaining for the absolute theory, the letter suggested a change in U.S. policy. *See id.*

26. *See* Tate Letter, *supra* note 25.

27. *See* Verlinden B.V. v. Central Bank of Nigeria, 461 U.S. 480, 487 (1983); Dorsey, *supra* note 16, at 258; Nicholas J. Evanoff, *Direct Effect Jurisdiction Under the Foreign Sovereign Immunities Act of 1976: Ending the Chaos in the Circuit Courts*, 28 HOUS. L. REV. 629, 633 (1991).

State Department to suggest immunity in cases where it should not have been available.[28] In addition, courts were generally left with little guidance to determine the existence of immunity without clear indication from the State Department.[29] Ultimately, determinations of immunity were being "made in two different branches, subject to a variety of factors, sometimes including diplomatic considerations."[30] Private parties who had chosen to deal with foreign governments were subjected to governing standards that were unclear and inconsistently applied.[31]

This uncertainty eventually led the State Department, along with the Justice Department, to propose a bill codifying the restrictive theory of sovereign immunity.[32] The resulting legislation set forth standards governing the circumstances under which private parties can maintain a lawsuit against a foreign state or its entities in the courts of the United States.[33]

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28. *See* STEVENSON ET AL., *supra* note 2, at 15 (noting that improper grants of immunity often resulted when governments pressured the State Department to recognize sovereign immunity).

29. *See Verlinden*, 461 U.S. at 487; GORDON, *supra* note 19, at 4-2. Ideally, the State Department intended to make determinations regarding sovereign immunity and then communicate them to courts. *See* GORDON, *supra* note 19, at 4-2. However, this practice was not necessarily followed. *See id.* In situations where the State Department felt that a request for immunity should be denied, it usually informed the foreign embassy but not the court. *See id.* Without information regarding the State Department's determination, courts did not know if the State Department had considered the request and rejected it, or not considered it at all. *See id.* The State Department's failure to communicate made it difficult for courts to defer to determinations that immunity should be denied. *See id.*

30. *Verlinden*, 461 U.S. at 488.

31. *See id.*

32. *See* DELLAPENNA, *supra* note 25, at 8.

33. *See* Foreign Sovereign Immunities Act of 1976, H.R. REP. No. 94-1487, at 8 (1976), *reprinted in* 1976 U.S.C.C.A.N. 6604. The standards set forth in the FSIA were intended to be the "sole and exclusive standards to be used in resolving questions of sovereign immunity raised by foreign states before Federal and State courts in the United States." *Id.* at 6610. As such, the Act preempts all other state and federal law regarding the issue of immunity of foreign states with the exception of international agreements. *See* GORDON, *supra* note 19, at 6-3.

C. CODIFICATION OF RESTRICTIVE IMMUNITY: THE FOREIGN SOVEREIGN IMMUNITIES ACT AND THE COMMERCIAL ACTIVITIES EXCEPTION

The Foreign Sovereign Immunities Act of 1976 (FSIA)[34] had four objectives: (1) to codify the restrictive principle of sovereign immunity; (2) to insure that the principle of restrictive immunity was used in U.S. courts; (3) to provide a statutory procedure for making service upon and obtaining in personam jurisdiction over a foreign state; and (4) to provide a remedy for a post-judgment creditor if a foreign state failed to satisfy a final judgment.[35] As a codified theory of restrictive immunity, the FSIA was designed to balance the competing interests in providing American individuals with a forum to adjudicate commercial disputes and the interests of foreign governments in being free from excessive litigation.[36]

Under the FSIA's theory of restrictive immunity, a sovereign state is immune from suit unless its activities fall within an enumerated set of exceptions.[37] One of the most commonly invoked is the commercial activity exception,[38] which poses two requirements: the sovereign state must engage in a commercial activity;[39] and the commercial activity must, at a minimum,

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34. 28 U.S.C. §§ 1330, 1602-1611 (1994).

35. *See* H.R. REP. NO. 94-1487, at 7, 8 (1976), *reprinted in* 1976 U.S.C.C.A.N. 6604.

36. *See* Donoghue, *supra* note 23, at 520-21; *see also Colonial Bank v. Compagnie Generale Maritime et Financiere*, 645 F. Supp. 1457, 1465 (S.D.N.Y. 1986) (warning that without some limit on the jurisdictional reach of U.S. courts, the "proclivity of the United States population to devise lawsuits for every contretemps" would subject foreign sovereigns to excessive litigation).

37. *See* 28 U.S.C. § 1604. Section 1605 contains seven classes of exceptions to immunity from jurisdiction. These exceptions encompass several different situations, ranging from waiver of immunity, participation in commercial markets and contested rights in property, to money damages and liens on maritime property. *See id.* §1605(a)(1)-(7).

38. *See id.* § 1605(a)(2). The statute provides:

> [A foreign state shall not be immune from the jurisdiction of courts of the United States or of the States 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.

39. *See id.* Whether a sovereign's activities are characterized as "commercial" depends on whether the underlying acts are considered "public," in which case immunity is available, or "private," in which case the commer-

cause a "direct effect" in the United States.[40] The "direct effect" language, however, has been referred to as a "problematic phrase"[41] because it does not provide a clear standard for determining what types of effects are sufficient to subject foreign governments to jurisdiction in U.S. courts.[42]

D. INTERPRETING THE DIRECT EFFECT CLAUSE: NARROW VERSUS BROAD INTERPRETATIONS AND THE SUPREME COURT'S DECISION IN *REPUBLIC OF ARGENTINA V. WELTOVER, INC.*

Congress did not provide a definition of "direct effect" in the FSIA, and there is little legislative history regarding the meaning of the clause. It is discussed in one short, non-specific paragraph of a House Report.[43] The House Report suggests that courts determine jurisdiction based on the principles set forth in section eighteen of the *Restatement (Second) of Foreign Relations*, but does not articulate a clear standard of its own.[44]

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cial activity exception applies. Courts have employed two different doctrines in making this distinction. The first is the "nature" test, which is "an objective inquiry into whether the act could be performed by a private or ordinary person." DELLAPENNA, *supra* note 25, at 148. If the act is such that an ordinary or private citizen could perform it, it is a "private" *commercial* act and the state will not be entitled to immunity. *See id.* If, however, the act is one that only a public authority could perform, it is a public *governmental* act and immunity is available. *See id.* The second doctrine is the "purpose" test, under which "an act is private or public according to whether it serves a public or private purpose." *See id.* Although authorities do not generally agree on what constitutes a public purpose, a state's contract is arguably immune from suit if it serves a public purpose and can be considered an act of government. *See id.* If, however, it is intended to have a commercial effect, then the foreign state is not immune from suit. *See id.*

Congress tried to clarify this confusion by declaring in the FSIA that "[t]he commercial character of an activity shall be determined by reference to the *nature* of the course of conduct . . . rather than by reference to its purpose." 28 U.S.C. §1603(d) (emphasis added). However, the explanation and examples of what constitutes a "commercial activity" provided by Congress did not completely resolve the issue. Courts still are not consistent in deciding whether particular transactions are commercial. *See* DELLAPENNA, *supra* note 25, at 152.

40. 28 U.S.C. § 1605(a)(2).

41. Tex. Trading & Milling Corp. v. Federal Republic of Nigeria, 647 F.2d 300, 311-312 (2d Cir. 1981).

42. *See* Gohlke, *supra* note 21, at 271.

43. H.R. REP. NO. 94-1487, at 19 (1976), *reprinted in* 1976 U.S.C.C.A.N. 6618.

44. The House envisioned that the direct effect clause "would embrace commercial conduct abroad having direct effects within the United States which would subject such conduct to the exercise of jurisdiction by the United States consistent with principles set forth in section 18, Restatement of the

Given this scant guidance as to the meaning of the clause, it is no surprise that circuit courts have interpreted the "direct effect" language in different ways.[45] The majority of courts have adopted a narrow view, accepting the language of section eighteen and finding that the term "direct effect" requires a substantial impact in the United States that is a directly foreseeable result of the extraterritorial conduct.[46] The Second

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Law, Second, Foreign Relations Law of the United States." H.R. REP. NO. 94-1487, at 19 (1976), *reprinted in* 1976 U.S.C.C.A.N. 6618; *see also* DELLAPENNA, *supra* note 25, at 90-92; Evanoff, *supra* note 27, at 637 ("The only interpretive guidance provided the courts as to the meaning of 'direct effect in the United States' is a cryptic reference to section 18 .... This lack of guidance ... has led to considerable confusion and divergence of opinion, first in the district courts, and now in the circuit courts.").

According to section 18, "a state has jurisdiction to prescribe a rule of law attaching legal consequences to conduct that occurs outside its territory and causes an effect within its territory, if ... the effect within the territory is substantial and occurs as a direct and foreseeable result of the conduct outside the territory." RESTATEMENT (SECOND) OF FOREIGN RELATIONS LAW OF THE UNITED STATES § 18 (1965). Thus, a foreign state is not liable for an effect in the United States unless the effect is direct, substantial, and foreseeable. *See id.*

45. *See* Gohlke, *supra* note 21, at 274 (discussing the emergence of two different views of the meaning of "direct effect in the United States" in the circuit courts).

46. *See* Gould, Inc. v. Pechiney Ugine Kuhlmann, 853 F.2d 445, 453 (6th Cir. 1988) (holding that a foreign state's commercial activity may satisfy the direct effect clause if the consequences of the extraterritorial act were the foreseeable result of the conduct); Callejo v. Bancomer, S.A., 764 F.2d 1101, 1111 (5th Cir. 1985) (relying on section 18 to determine that "the conduct must have a 'substantial' effect in the United States 'as a direct and foreseeable result of the conduct'" outside the United States) (citation omitted); Berkovitz v. Islamic Republic of Iran, 735 F.2d 329, 332 (9th Cir. 1984) (stating that effects on the family of an American citizen who was murdered in Iran were "not sufficiently 'direct' or 'substantial' to support the assertion of Federal jurisdiction") (quoting Verlinden B.V. v. Central Bank of Nigeria, 488 F. Supp. 1284, 1298 (S.D.N.Y. 1980), *aff'd on other grounds*, 647 F.2d 320 (2d Cir. 1981), *rev'd on other grounds*, 461 U.S. 480 (1983)) (footnote omitted); Maritime Int'l Nominees Establishment v. Republic of Guinea, 693 F.2d 1094, 1111 (D.C. Cir. 1982) (stating that "an effect cannot be deemed direct if it occurs solely because of conduct not reasonably contemplated by the commercial activity"); Harris Corp. v. Nat'l Iranian Radio & Television, 691 F.2d 1344, 1351 (11th Cir. 1982) (holding that the breach of a letter of credit involved in the sale of radio transmitters from overseas producers fell within the commercial activity exception because it had "significant, foreseeable ... consequences" in the United States); Harris v. VAO Intourist, 481 F. Supp. 1056, 1062-63, 1065 (E.D.N.Y. 1979) (holding that an American citizen's death in a Moscow hotel fire was an inadequate basis for jurisdiction under the direct effect requirement). *See generally* DELLAPENNA, *supra* note 25, at 90-91. Dellapenna notes, however, that even in the cases in which courts have relied upon the language of section 18, the courts did "no more than quote it without

Circuit, by contrast, has eschewed the majority approach in favor of a narrower view.[47] After considering the House Report's reference to section eighteen, the Second Circuit noted that the section concerned "the extent to which . . . American law may be applied to conduct overseas, not the . . . extraterritorial jurisdictional reach of American courts."[48] Concluding that the "substantial" and "foreseeable" requirement of section eighteen was "not necessarily apposite to the direct effect clause,"[49] the Second Circuit articulated its own version of the direct effect test.[50] The Second Circuit's test focused on whether an effect was "sufficiently 'direct' and sufficiently 'in the United States' that Congress would have wanted an American court to hear the case."[51]

The circuit split between the narrow and broad view eventually prompted the Supreme Court to attempt to settle the confusion surrounding direct effect jurisdiction in *Republic of Argentina v. Weltover, Inc.*[52] *Weltover* involved a suit brought by several bondholders against the Republic of Argentina for breach of contract.[53] The case turned on the question whether

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examining the extensive underlying international practice that the section seeks to summarize." *Id.* at 91. Due to the courts' failure in examining this body of knowledge, Dellapenna argues that section 18 "is little help, without reference to the underlying international practice, in deciding specific cases." *Id.*

47. *See* Tex. Trading & Milling Corp. v. Federal Republic of Nigeria, 647 F.2d 300, 313 (2d Cir. 1981). *Texas Trading* involved four trading companies that had contracted to sell and deliver shiploads of cement to the government of Nigeria during the late 1970s. *See id.* at 302-03. Nigeria entered into over one hundred contracts with sixty-eight cement suppliers at a total value of almost one billion dollars. *See id.* at 303. The quantities of cement purchased were so great that Nigeria's docks soon became inundated with cement-laden ships, filling the harbors to such an extent that imports of other essential goods were forced to cease. *See id.* at 302. Faced with a crisis, the Nigerian Government repudiated all unperformed cement contracts. *See id.* When the plaintiffs, whose cement contracts had been repudiated, brought suit in New York, Nigeria moved for dismissal based on its alleged immunity as a foreign sovereign. *See id.* The court, however, held that Nigeria was not entitled to immunity, basing jurisdiction on the financial loss suffered by the American corporation. *See id.* at 312.

48. *Id.* at 311.

49. *Id.* at 311 n.32.

50. *See id.* at 313.

51. *Id.*

52. 504 U.S. 607 (1992).

53. *Id.* at 607. In 1981 the Argentine Government instituted the Foreign Exchange Insurance Contract program (FEIC) in an attempt to remedy the instability of its currency. *See id.* at 609. Under the FEIC, Argentina and its

Argentina's unilateral rescheduling of its debt resulted in a direct effect in the United States sufficient to support jurisdiction under the FSIA.[54] Like many of the circuit courts that had decided the issue, the Supreme Court first considered the House Report's suggestion that the clause be interpreted based on the principles set forth in section eighteen of the Restatement.[55] Consistent with the Second Circuit, the Supreme Court noted the inconsistency between the section eighteen concept of jurisdiction to legislate and the FSIA's concern with jurisdiction to adjudicate.[56] The Court then rejected the suggestion in the legislative history that the commercial activity exception contains an unexpressed requirement of "substantiality" or "foreseeability."[57] Instead, the Supreme Court adopted the direct effect test originally suggested by the Second Circuit.[58]

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central bank assumed the risk of currency depreciation in cross-border contracts between Argentine borrowers and foreign creditors by providing the domestic borrowers with U.S. dollars to pay their international debts. *See id.* When the contracts later came due in 1982, currency devaluation had depleted Argentina's funds to such an extent that it could not cover the contractual obligations. *See id.* As an emergency measure, the Argentine government refinanced some of its debts by issuing government bonds (called "Bonods") to certain creditors. *See id.* Interest and principal payments on the bonds were to be paid in U.S. dollars through banks in New York, Frankfurt, London, or Zurich at the bondholder's option. *See id.* at 609-10. However, when the bonds matured in 1986, the Argentine government again lacked sufficient hard currency reserves to retire them, so it unilaterally rescheduled repayment. *See id.* The plaintiffs refused to accept Argentina's rescheduling of the payments and insisted on full repayment in New York according to the instruments' original terms. *See id.* When no payments were made, the plaintiffs brought the action to compel the Argentine government to honor its obligations. *See id.*

54. *See id.* at 617. Another issue the Supreme Court considered was whether Argentina's default on the bonds was an act performed in connection with a commercial activity. *See id.* at 612. Argentina argued that issuance of the bonds should not be characterized as commercial activity because the instruments were not used in a commercial context. *See id.* at 615-16. Instead, it argued, the instruments "were created by the Argentine Government to fulfill its obligations under a foreign exchange program designed to address a domestic credit crisis, and as a component of a program designed to control that nation's critical shortage of foreign exchange." *Id.* at 616. The Court responded by saying that it did not matter *why* Argentina participated in the bond market as a private actor, only that it did so. *See id.* at 617.

55. *See id.* at 617-18.

56. *See id.* at 618; *supra* text accompanying notes 47-51 (discussing the Second Circuit's approach).

57. *See Weltover*, 504 U.S. at 618.

58. *See id.* at 619. The test provided by the Second Circuit states that an effect is direct if it follows as an immediate consequence of the defendant's activity. *See* Weltover, Inc. v. Republic of Argentina, 941 F.2d 145, 152 (2d

Using this test, the Supreme Court easily concluded that Argentina's unilateral rescheduling of the maturity dates on its government bonds had a direct effect in the United States.[59]

E. THE AFTERMATH OF *WELTOVER*: SUBSEQUENT INTERPRETATIONS IN CIRCUIT COURTS

Although the *Weltover* decision represented an attempt to clarify the ambiguity surrounding the direct effect language of the commercial activity exception, the Supreme Court failed to offer future courts any clear direction.[60] Application of the direct effect clause in subsequent cases has proven to be varied and unpredictable, with at least one court admitting that it "struggled to identify objective standards that would aid in determining what does and does not qualify as a 'direct effect in the United States.'"[61]

Lacking the guidance of the "substantial" and "foreseeable" test adopted by many courts prior to *Weltover*, and faced with a Supreme Court decision that seemed "hopelessly ambiguous,"[62] several courts looked for a more definitive standard to help determine what qualifies as a direct effect.[63] As a result, the Second, Eighth, Ninth, and Tenth Circuits grafted a new requirement onto the direct effect test.[64] Under their new standard, a

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Cir. 1991), *aff'd*, 504 U.S. 607 (1992).

59. *See Weltover*, 504 U.S. at 618-19. According to the Court's reasoning, the fact that New York was the place of performance for the contract was the decisive factor in deciding whether a direct effect occurred in the United States. *See id.* at 619. When Argentina failed to honor the bonds, money that was supposed to have been delivered to a New York bank for deposit was not forthcoming. *See id.*

The Court rejected the argument advanced by Argentina that the direct effect requirement cannot be satisfied where the plaintiffs are all foreign corporations. *See id.* at 618-19. Relying on its decision in *Verlinden B.V. v. Central Bank of Nigeria*, 461 U.S. 480 (1983), the Court noted that the FSIA "permits 'a foreign plaintiff to sue a foreign sovereign in the courts of the United States, provided the substantive requirements of the Act are satisfied.'" *Weltover*, 504 U.S. at 619 (quoting *Verlinden*, 461 U.S. at 489).

60. *See* Gohlke, *supra* note 21, at 285; Lew, *supra* note 24, at 774-75.

61. United World Trade, Inc. v. Mangyshlakneft Oil Prod. Ass'n, 33 F.3d 1232, 1237 (10th Cir. 1994).

62. *Id.*

63. Although the court in *United World Trade* felt as though it were left with little direction to determine what qualifies as a direct effect, it noted that it would consider the Supreme Court's example in *Weltover* while applying the statute to the facts before it. *See id.*

64. *See* Antares Aircraft, L.P. v. Federal Republic of Nigeria, 999 F.2d 33 (2d Cir. 1993); General Elec. Capital Corp. v. Grossman, 991 F.2d 1376 (8th

foreign sovereign is not subject to jurisdiction under the commercial activity exception unless it has engaged in a "legally significant act" in the United States.[65] Courts have generally defined "legally significant act" as an act giving rise to a cause

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Cir. 1993); Adler v. Federal Republic of Nigeria, 107 F.3d 720 (9th Cir. 1997); United World Trade, Inc. v. Mangyshlakneft Oil Prod. Ass'n, 33 F.3d 1232 (10th Cir. 1994). *Antares Aircraft* involved an action brought by an American Partnership against the Federal Republic of Nigeria for conversion of an airplane. 999 F.2d at 34. After the plane was finally returned, Antares filed an action in New York to recover damages for conversion of the plane, arguing that their financial loss as a result of the tort constituted a direct effect that occurred in the United States. *See id.* at 36. However, the court refused to exert jurisdiction because all of the legally significant acts took place in Nigeria. *See id.*

The Eighth Circuit encountered the direct effect clause in *General Electric Capital Corporation v. Grossman*, a case involving an action brought by General Electric, Gelco, and International Couriers Corporation against Air Canada and some Canadian accounting partnerships. 991 F.2d at 1378. The plaintiffs claimed that the defendants conspired to suppress information about Gelco's financial status in order to dupe General Electric into buying the company at an inflated price. *See id.* at 1379. The court agreed with the defendant's claim of immunity, and dismissed the case due to a lack of jurisdiction. *See id.* at 1384.

The Ninth circuit interpreted the direct effect language in *Adler v. Federal Republic of Nigeria*, a case involving an action brought by an assignee over the right to receive payment on a Nigerian government contract to computerize oil fields. 107 F.3d at 720. When the Nigerian government failed to pay the money, Adler filed suit in New York for breach of contract, arguing that Nigeria's failure to make payment to his account in New York caused a direct effect in the United States. *See id.* at 723. The court denied Nigeria sovereign immunity under the FSIA, concluding that Nigeria engaged in a legally significant act in the United States. *See id.* at 730.

United World Trade, Inc. v. Mangyshlakneft Oil Production Association, a case decided by the Tenth Circuit, involved a complex agreement for the sale of oil. 33 F.3d at 1235. UWT entered into an agreement with MOP to the effect that MOP would provide UWT with shipments of crude oil. *See id.* UWT contracted to make payment to MOP in U.S. dollars by irrevocable letters of credit opened by a European/USA bank and notified through an advising bank. *See id.* Although the first two shipments went smoothly, a problem arose with the third shipment. *See id.* at 1236. MOP thereafter refused to supply any additional oil to UWT. *See id.* UWT then brought suit in Colorado for breach of contract, alleging jurisdiction based on the direct effect clause. *See id.* UWT contended that there was a direct effect in the U.S. because money that was supposed to have been paid in the United States was not transferred because of defendant's breach of contract. *See id.* at 1237. Distinguishing the case from *Weltover*, the court noted that "no part of the contract in this case was to be performed in the United States." *Id.* The court concluded that MOP was immune from jurisdiction because all of the legally significant acts occurred in Europe and not in the United States. *See id.* at 1239.

65. *See Antares Aircraft*, 999 F.2d at 36; *General Elec. Capital Corp.*, 991 F.2d at 1385; *Adler*, 107 F.3d at 730; *United World Trade*, 33 F.3d at 1237-38.

of action in U.S. courts.[66] In other words, an act has "legal significance" only if the aggrieved party can show that the foreign government engaged in some activity *in the United States* which, jurisdictional issues aside, would support a cause of action in our courts.[67] The legally significant act requirement obviously makes it more difficult to grant jurisdiction over foreign governments;[68] as one circuit court put it, it is designed to prevent interpretations of the direct effect clause "that would give the district courts jurisdiction over virtually any suit arising out of an overseas transaction in which an American citizen claims to have suffered a loss from the acts of a foreign state."[69]

Although the legally significant act requirement does provide a uniform standard for granting sovereign immunity, it has generated concern over American business interests.[70] The requirement is arguably more protective of foreign governments, and makes it slightly more difficult to obtain jurisdiction over a sovereign entity.[71] As one critic has pointed out, re-

66. *See, e.g., Adler*, 107 F.3d at 727.

67. *See supra* note 64 and accompanying text. For example, the Tenth circuit in *United World Trade* considered it significant that "no part of the contract involved in [the] case was to be performed in the United States." 33 F.3d at 1237. The "legally significant acts" were the contract entered into by UWT and MOP in Moscow, the delivery of oil from Kazakhstan to Sicily, and the payments by UWT to MOP in Paris. *See id.* at 1239. Thus, because none of the acts giving rise to the cause of action actually occurred in the United States, there was no "direct effect" in the United States. *See id.*

68. *See* Voest-Alpine Trading USA Corp. v. Bank of China, 142 F.3d 887, 896 (5th Cir. 1998) (noting that the Supreme Court in *Weltover* "admonished the circuit courts not to add 'any unexpressed requirement[s]' to the third clause," and arguing that the legally significant act analysis adds an unexpressed requirement). The language in some of the circuit court opinions also suggests that the courts were looking for a standard that would limit jurisdiction in certain circumstances. *See, e.g., Antares Aircraft*, 999 F.2d at 36 (noting that "the fact that an American individual or firm suffers some financial loss from a foreign tort cannot, standing alone, suffice to trigger the exception"); *United World Trade*, 33 F.3d at 1238 (concluding that it was not the intent of Congress "to provide jurisdiction whenever the ripples caused by an overseas transaction manage eventually to reach the shores of the United States").

69. *United World Trade*, 33 F.3d at 1239.

70. *See generally* Dean Brockbank, Comment, *The Sovereign Immunity Circle: An Economic Analysis of* Nelson v. Saudi Arabia *and the Foreign Sovereign Immunities Act*, 2 GEO. MASON L. REV. 1 (1994) (discussing the economic ramifications of grants of immunity on American companies and individuals transacting business with foreign countries).

71. *See Voest-Alpine*, 142 F.3d at 894 (referring indirectly to the legally significant act requirement as an additional unexpressed requirement to the commercial activity exception).

cent interpretations of the commercial activity exception "have granted immunity as the rule rather than the exception."[72] Proponents of American business interests argue that grants of immunity should be limited in order to provide more protection for the U.S. economic system.[73] The increased threat of nonrecourse in dealings with foreign governments ultimately raises the risks of foreign investment and introduces inefficiencies into the bargaining process.[74] These potential pitfalls implicitly factored into the Fifth Circuit's rejection of the legally significant act requirement in *Voest-Alpine Trading USA Corp. v. Bank of China*.[75]

II. *VOEST-ALPINE TRADING USA CORP. V. BANK OF CHINA*

The Fifth Circuit's recent decision in *Voest-Alpine Trading USA Corp. v. Bank of China*[76] departed significantly from the reasoning employed by the Second, Eighth, Ninth, and Tenth circuits.[77] Unlike the other circuits, the Fifth Circuit relied on a more literal interpretation of the direct effect clause.[78] Thus, rather than adopting the legally significant act requirement, the court looked back to the interpretive language originally set forth in *Weltover*, which held that "an effect is 'direct' if it follows 'as an immediate consequence of the defendant's . . . activity' and it need not be foreseeable nor substantial."[79]

Voest-Alpine refused to adopt the legally significant act requirement developed by the other circuits for two reasons. First, the Fifth Circuit carefully analyzed the language of the direct effect clause and concluded that the text of the FSIA does not support the legally significant act requirement.[80]

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72. Brockbank, *supra* note 70, at 12.

73. *See id.* at 20.

74. *See id.* at 21-23.

75. 142 F.3d 887, 897 (5th Cir. 1998). Although the Fifth Circuit never makes an explicit reference, the language indirectly suggests that the decision is intended to be protective of American interests. The holding refers specifically to "American" plaintiffs and corporations, and wipes away what is considered an extra, "unexpressed" component of the FSIA. *See id.* at 894-95, 897.

76. 142 F.3d 887 (5th Cir. 1998).

77. *See* discussion *supra* Part I.E.

78. *See Voest-Alpine*, 142 F.3d at 894-95.

79. *Id.* at 894 (quoting Republic of Argentina v. Weltover, Inc., 504 U.S. 607, 618 (1992)) (citation omitted).

80. *See id.* at 894.

Utilizing a strictly textual interpretation, the court reasoned that the only act that must "give rise to or form the basis of the cause of action is an act *outside* the United States."[81] In support of its contention, the *Voest-Alpine* court noted that the "Supreme Court [in *Weltover*] expressly admonished the circuit courts not to add 'any unexpressed requirement[s]' to the [direct effect] clause."[82] Because the legally significant act requirement was never expressed in the third clause of the commercial activity exception, it should not have been added to the direct effect provision.[83]

Second, the Fifth Circuit contended that the legally significant act requirement merges the second and third clauses of the commercial activity exception.[84] The court found that, in effect, both the second clause and the legally significant act requirement base jurisdiction on acts in the United States which would give rise to a cause of action.[85] Therefore, if the third clause is interpreted to require a legally significant act in the United States, the second and third clauses become virtually indistinguishable.[86] The court determined that Congress did not intend such a "meaningless construction" of the third clause of the commercial activity exception, and refused to adopt the legally significant act requirement.[87]

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81. *Id.*

82. *Id.*

83. *See id.* Although the other circuits noted that the Supreme Court employed an analysis similar to the legally significant acts test in deciding *Weltover*, the Fifth Circuit argued that "*Weltover*'s reliance on a legally significant act in the United States does not justify, much less compel, the conclusion that it is or should be some kind of threshold requirement under the third clause." *Id.* (citation omitted). Therefore, the court concluded, although "[a] legally significant act in the United States will certainly cause a direct effect in the United States . . . that does not mean that a direct effect in the United States can be caused *only* by a legally significant act in the United States." *Id.*

84. *See id.* at 895.

85. *See id.* The second clause requires that a cause of action be based upon (1) an act in the United States (2) in connection with commercial activity outside the United States. *See* 28 U.S.C. § 1605 (a)(2) (1994).

86. *See Voest-Alpine*, 142 F.3d at 895. The court noted, however, that the clauses may be distinguished by the fact that the third clause would also "require proof of an act outside the United States upon which the action is also based and which caused a direct effect in the United States." *Id.* This interpretation, however, would leave the third clause with no clear purpose because it would be easier for plaintiffs to invoke the second clause, as it would not have the extra requirement. *See id.* Thus, the court concluded that this interpretation would be useless. *See id.*

87. *Id.*

Rather than rely on the legally significant act requirement, the court in *Voest-Alpine* adopted the test set forth in *Weltover*, which required that an effect in the United States need only be an immediate consequence of the foreign state's activity.[88] The Fifth Circuit also cited its earlier decision in *Callejo v. Bancomer, S.A.*,[89] where it held that "a financial loss incurred in the United States by an American plaintiff may constitute a direct effect that supports jurisdiction under the third clause."[90] More specifically, the court relied on *Callejo* as support for the idea that the place of payment and the amount of contact between a foreign state and the United States were not decisive factors in the direct effect analysis.[91]

Applying these prior decisions, the Fifth Circuit concluded that Voest-Alpine suffered a "nontrivial" financial loss in the United States when it did not receive payment from the Bank of China.[92] Furthermore, Voest-Alpine's nonreceipt of funds occurred "as an 'immediate consequence' of the Bank of China's actions."[93] As a result, the loss was sufficient to support jurisdiction under the third clause of the commercial activity exception.[94] In a much broader sense, *Voest-Alpine* established that a financial loss suffered by an American plaintiff in the United

88. *See Weltover*, 504 U.S. at 618.

89. 764 F.2d 1101 (5th Cir. 1985).

90. *Voest-Alpine*, 142 F.3d at 893 (describing its holding in *Callejo*). *Callejo* involved a breach of contract action arising from the promulgation by Mexico of exchange rate control regulations. 764 F.2d at 1104. The plaintiffs sought payment on four certificates of deposit and received a rate of exchange substantially below the market rate. *See id.* at 1106. In analyzing whether Mexico's commercial activity had a direct effect in the United States, the court concluded that the place of payment was not decisive. *See id.* at 1112. However, after examining the longstanding business relationship between the parties, and the substantial harm suffered by the plaintiffs, the court ultimately found that Mexico's activities did have a direct effect in the United States. *See id.*

91. *See Voest-Alpine*, 142 F.3d at 895-96. *Callejo* clearly asserts that continuous contact is not important in the context of an FSIA analysis. 764 F.2d at 1112. Continuous contact *is* likely to be important, however, in establishing "minimum contacts" for traditional personal jurisdiction purposes. *See, e.g.*, General Elec. Capital Corp. v. Grossman, 991 F.2d 1376, 1387 (8th Cir. 1993) (discussing personal jurisdiction and the "minimum contacts" test). Thus, by suggesting that the amount of contact is inconsequential in a direct effect analysis, *Callejo* establishes a standard for jurisdiction that is set even lower than the minimum contacts standard.

92. *Voest-Alpine*, 142 F.3d at 896.

93. *Id.* (quoting the Supreme Court's language in *Weltover*, 504 U.S. at 618).

94. *See id.*

States, if it is an immediate consequence of the defendant's activity, is sufficient to support jurisdiction under the third clause of the commercial activity exception to the FSIA.[95]

III. DEPARTING FROM LEGALLY SIGNIFICANT ACTS: WHY *VOEST-ALPINE*'S INTERPRETATION OF THE COMMERCIAL ACTIVITY EXCEPTION SPELLS TROUBLE FOR OVERSEAS TRANSACTIONS

Voest-Alpine set forth a broad standard for determining jurisdiction in cases involving commercial transactions between foreign sovereigns and American corporations.[96] Although the decision represents a fair attempt at interpreting Supreme Court precedent, the Fifth Circuit's approach to the commercial activity exception may have a negative impact on international transactions. *Voest-Alpine*'s strict adherence to the original language of *Weltover* and reliance on its earlier opinion in *Callejo* establishes a standard that is heavily "skewed toward granting jurisdiction over foreign states."[97] The direct effect clause should be read to include established standards so that subsequent interpretations do not turn our courts into "small international courts of claims."[98]

A. REJECTING THE LEGALLY SIGNIFICANT ACT REQUIREMENT

Although the Second, Eighth, Ninth, and Tenth Circuits had applied the legally significant act requirement in previous cases,[99] *Voest-Alpine* refused to adopt the standard.[100] The court found that the legally significant act requirement was not supported by the text of the FSIA, and that it rendered the second and third provisions of the commercial activity exception virtually indistinguishable.[101] However, the court's arguments are based on mistaken assumptions. Nothing in the language of the FSIA or *Weltover* actually prohibits the use of this addi-

95. *See id.* at 897.

96. *See supra* Part II.

97. Gohlke, *supra* note 21, at 283.

98. *Id.* at 284 (quoting *Jurisdiction of U.S. Courts in Suits Against Foreign States: Hearings Before the Subcomm. on Administrative Law and Governmental Relations of the House Comm. on the Judiciary*, 94th Cong., 2d Sess. 25, 31 (1976) (testimony of Bruno A. Ristau)).

99. *See supra* note 64 and accompanying text.

100. *See supra* notes 79-87 and accompanying text.

101. *See Voest-Alpine*, 142 F.3d at 894; *see also supra* notes 85-93 and accompanying text.

tional standard. Furthermore, the legally significant act requirement focuses on entirely different "acts" than the second clause of the commercial activity exception.

1. Misinterpreting the Words of *Weltover*

Voest-Alpine misinterpreted the language of *Weltover* by suggesting that the legally significant act requirement should be rejected because it was not explicitly provided for in the text of the FSIA.[102] While the Supreme Court "reject[ed] the suggestion that section 1605(a)(2) contains any unexpressed requirement of 'substantiality' or 'foreseeability,'"[103] *Weltover* did not prohibit the addition of *any* requirement not expressed in the text of the FSIA.[104] The Supreme Court only addressed the suggestion that the direct effect clause would be subject to jurisdiction consistent with the principles of section eighteen of the *Restatement (Second) of Foreign Relations*.[105] Thus, *Weltover* rejected the idea that an effect is only "direct" if it results from conduct that has, "as a direct and foreseeable result, a 'substantial' effect within the United States."[106] The Court was not considering the possibility that circuit courts would adopt a requirement that acts as a guideline for future interpretation of the direct effect clause.[107]

Although *Weltover* indicated the Supreme Court's intent to eliminate the "substantiality" and "foreseeability" requirements,[108] the legally significant act requirement should not be equated with these tests. The requirement differs significantly from the principles rejected in *Weltover*. While the "foreseeability" and "substantiality" requirements tend to concentrate on the impact of the activity[109] and whether the parties

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102. *See supra* notes 80-83 and accompanying text.

103. *Weltover*, 504 U.S. at 618.

104. *See id.*

105. *See supra* notes 55-56 and accompanying text.

106. *Weltover*, 504 U.S. at 618.

107. Although the language used by Supreme Court, if read broadly, could be interpreted as rejecting any requirements involving any type of "substantiality" or "foreseeability" requirement, this interpretation is not consistent with the flow of the Court's argument. The text immediately preceding this assertion clearly refers to the requirements as explained in the Restatement, so the Court is quite clearly referring to these principles rather than making a general assertion. *See Weltover*, 504 U.S. at 618.

108. *See supra* notes 57-58 and accompanying text.

109. The test bases extraterritorial application on whether an act had a "substantial" effect in the United States, which suggests that there is a quan-

contemplated the effects of the activity,[110] the legally significant act requirement focuses on the activity's connection with the United States.[111] If a foreign state's involvement in commercial markets leads to an actionable claim, the court will grant jurisdiction if the cause of action establishes that something legally significant actually occurred in the United States.[112] This requires an aggrieved party to demonstrate that a major event in the commercial dispute, i.e., the making of a contract, or the failure to uphold the obligations of a contract, had a direct connection to the United States.[113] This position is clearly consistent with the reasoning of *Weltover*. The Court's rejection in that case of the "substantiality" and "foreseeability" requirements in favor of the "immediate consequences" test suggests that the Court did not want a test based solely on the impact of the commercial act in the United States.[114] Instead, the Court focused on the existence of a direct connection between the foreign state's activity and the effect in the United States.[115] The language of the Court's test demonstrates this shift in focus: "an effect is 'direct' if it follows 'as an immediate consequence of the defendant's activity.'"[116] Therefore, unlike the substantiality and foreseeability tests, the legally significant act requirement is a logical extension of the Court's conclusion in *Weltover*. Jurisdiction is essentially limited to situations in which a foreign state's misconduct is sufficiently connected to, and results in, a direct effect in the United States. Collateral effects of the activity are not sufficient to establish jurisdiction.[117]

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titative measure of the impact. *See* Gohlke, *supra* note 21, at 272-73.

110. *See id.*

111. For a more detailed discussion of this connection, see *infra* Part III.A.2.

112. *See supra* notes 66-67 and accompanying text.

113. *See supra* notes 66-67 and accompanying text.

114. Aside from noting that the two requirements were derived from a section of the Restatement that deals with jurisdiction to "legislate" rather than jurisdiction to "adjudicate," the Court never provided its reasons for rejecting the "substantiality" and "foreseeability" requirements. *See Weltover*, 504 U.S. at 617-18. However, after considering the aim of the "immediate consequences" test and the focus of the other requirements, it seems apparent that the Court did not want a test based solely on the impact of the commercial act in the United States.

115. *See id.*

116. *Id.* at 618 (quoting Weltover, Inc. v. Republic of Argentina, 941 F.2d 145, 152 (2d Cir. 1991)).

117. Secondary effects, such as those recognized in *United World Trade v.*

2. Failing to Distinguish the Second and Third Clauses of the Exception

Voest-Alpine's most compelling argument suggests that the legally significant act requirement merges the second and third clauses of the commercial activity exception.[118] While the court rightfully indicates that Congress would not condone a duplicative interpretation of the third clause, the court's analysis mischaracterizes the jurisdictional hook of the legally significant act requirement. Although the requirement focuses on the location of the "legally significant acts,"[119] and whether these acts bear some connection to the United States, the court failed to recognize the distinction between legally significant acts and the "act" in connection with a commercial activity used to determine the applicable provision of the commercial activity exception.[120] The second clause of the exception only applies when a foreign government engages in an activity within the United States that directly results in an actionable claim.[121] For example, if a foreign sovereign and an American corporation negotiate a contract in the United States, and the foreign government intentionally misrepresents its position, the activity would support jurisdiction under the second provision.[122] If, however, the parties negotiated outside of the U.S., the activity

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Mangyshlakneft Oil Production Association, are not sufficient to support jurisdiction. 33 F.3d 1232, 1238 (10th Cir. 1994). The contract in *United World Trade*, which was the basis for all of the "legally significant acts" of the foreign state, contained no express connection to the United States. *See id.* The defendants were not required to make payment in the United States, nor could they have anticipated what UWT expected to do with the money. *See id.* In other words, there was no legal obligation that connected the defendants to the United States. *See id.* Therefore, even though the breach of contract ultimately prevented UWT from collecting money in the United States, this "effect" was collateral to the primary cause of action. *See id.* The legally significant act—the failure to pay a London Bank pursuant to the contract—led to "immediate consequences" in Europe, not in the United States. *See id.*

118. *See supra* notes 84-87 and accompanying text.

119. *See supra* notes 65-67 and accompanying text.

120. The Fifth Circuit assumed that the basis of the cause of action is the only legally significant act that is considered. *See Voest-Alpine*, 142 F.3d at 895.

121. *See* 28 U.S.C. §1605(a)(2) (1994); *supra* note 38 (quoting the commercial activity exception).

122. *Cf.* General Elec. Capital Corp. v. Grossman, 991 F.2d 1376, 1384 (8th Cir. 1993) (rejecting the argument that the defendant's issuance of false financial information fell within the second clause because most of the negotiations and the underlying accounting and auditing problems took place outside the United States).

would not fall within the scope of the second clause because the actionable "act" did not occur in the U.S.[123] In this situation, the legally significant act requirement can be distinguished from the second clause of the exception. While the second clause is clearly not applicable, the outcome can still be decided using the legally significant act requirement. For example, if the contract between the foreign government and an American corporation contains no legal obligations connected to the United States, there is no legally significant act that would provide jurisdiction under the third clause of the exception.[124] However, if the contract provisions call for a stated event to occur within the United States, and the event does not occur as a result of the foreign government's misconduct, failure to satisfy the obligation constitutes a legally significant act.[125] Unlike the analysis under the second clause of the commercial activity exception, this finding does not require a foreign sovereign to actually engage in an activity within the United States.[126] Instead, jurisdiction results from the fact that the failure to uphold the contract provision would lead to a direct effect in the United States.[127]

Considering the legally significant act requirement in this sense, it is entirely possible to separate the "act" of the foreign state as it is necessary for determining which provision of the exception is applicable, from the "legally significant acts" that are useful in measuring whether there has been a "direct effect" in the United States.[128] The Supreme Court's decision in *Weltover* provides a good example.[129] *Weltover* was decided in the context of the third clause of the exception because it involved a contract that was conceived, entered into, and, for the

123. *See id.*

124. *See, e.g., United World Trade*, 33 F.3d at 1238 (refusing to grant jurisdiction because there was no legal obligation that connected defendants to the United States).

125. *See, e.g.*, Adler v. Federal Republic of Nigeria, 107 F.3d 720, 727 (9th Cir. 1997) (holding that Nigeria was subject to jurisdiction because its failure to deliver payment to a bank in the U.S. was legally significant).

126. Neither *Weltover* nor *Adler* dealt with the second clause because it was assumed that the foreign government did not engage in any activity in the United States. *See Weltover*, 504 U.S. at 619; *Adler*, 107 F.3d at 727.

127. *See Weltover*, 504 U.S. at 619; *Adler*, 107 F.3d at 727.

128. *See* cases cited *supra* note 64.

129. *Weltover* is useful because it has been cited for utilizing an analysis "similar" to the legally significant act requirement. *See* Antares Aircraft, L.P. v. Federal Republic of Nigeria, 999 F.2d 33, 36 (2d Cir. 1993).

most part, executed outside of the United States.[130] However, the decisive factor in the Court's analysis was the fact that the contract called for payment in the United States.[131] The Court focused on the contract's connection with the United States and placed a strong emphasis on the fact that payment that was supposed to have been received in New York never arrived according to the agreement.[132] This analysis is virtually identical to the legally significant act requirement.[133] Argentina's failure to fulfill its contractual obligation was a legally significant act that had a direct effect in the United States.[134] Nonperformance of the obligation to pay gave rise to a breach of contract cause of action.[135] Thus, the Supreme Court's analysis ultimately centered on the same basic premise of the legally significant act requirement; it simultaneously maintained the distinction between the second and third provisions of the commercial activity exception and implicitly focused on the "legally significant" connection between the commercial transaction and its domestic impact.[136]

B. *VOEST-ALPINE*'S RELIANCE ON *CALLEJO*: IS THERE ANY LIMIT TO JURISDICTION?

The Fifth Circuit's analysis of its previous decision in *Callejo v. Bancomer, S.A.*[137] is perhaps the most problematic aspect of *Voest-Alpine*. The court's interpretation of *Callejo* suggests that the amount of contact between a foreign sovereign and the United States is inconsequential in a direct effect analysis.[138] This assertion is troublesome because it marks an expansion of the jurisdictional reach of the FSIA. In essence, the court removed any standards that limit jurisdiction.[139]

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130. 504 U.S. at 609-10.

131. *See id.* at 618-19.

132. *See id.*

133. *See Antares Aircraft*, 999 F.2d at 36.

134. *See id.* According to the court in *Antares Aircraft*, "*Weltover* involved a breach of contract, and the Court found decisive the fact that the contractually designated place of performance was New York. The 'legally significant' act was thus the breach that occurred in the United States." *Id.*

135. *See id.*

136. *See Weltover*, 504 U.S. at 618-19.

137. 764 F.2d 1101 (5th Cir. 1985).

138. *See Voest-Alpine*, 142 F.3d at 895-96. For a background discussion of *Callejo*, see *supra* note 90.

139. *See supra* notes 88-95 and accompanying text.

By expanding the jurisdictional limits, the Fifth Circuit has radically altered the commercial activity exception. Under the court's formulation, the direct effect analysis favors jurisdiction over foreign states rather than preserving sovereign immunity.[140] As a substitute for traditional personal jurisdiction analysis, the "immediate consequences" test reaches significantly further than the minimum contacts standard.[141] In at least some cases granting jurisdiction, the plaintiffs would not have been able to establish minimum contacts.[142] In effect, the standard has been set so low that virtually any determination of jurisdiction will not constitute an abuse of discretion, whether or not jurisdiction is asserted over the foreign sovereign.[143]

Voest-Alpine's reliance on *Callejo* raises the question whether any limits to jurisdiction remain under the direct effect clause.[144] Critics of the *Weltover* decision would respond with an emphatic "no," arguing that the third clause of the commercial activity exception has been effectively reduced to a rubber stamp.[145] Any financial loss suffered by an American individual or corporation is likely to trigger the exception.[146] Whether or not this argument has merit, *Weltover* clearly lowered the standard for granting jurisdiction.[147] As a result, the

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140. *See* Gohlke, *supra* note 21, at 283.

141. *See* Lew, *supra* note 24, at 768-69. As Lew points out, "[b]y adopting a liberal standard for determining subject matter jurisdiction over U.S. lawsuits brought against non-U.S. governments, the [Supreme] Court indicated a desire to assert jurisdiction over a greater number of non-U.S. governments." *Id.*

142. *See* Wydeven, *supra* note 3, at 171-72.

143. *See* Gohlke, *supra* note 21, at 296.

144. *See id.*

145. *See, e.g.*, Gohlke, *supra* note 21, at 297 ("Had the FSIA been passed ten years later than it was, the Court may not have been able to so easily run roughshod over the intent of Congress."); Leacock, *supra* note 15, at 120-21 ("The Court's decision in *Republic of Argentina* [*v. Weltover, Inc.*] is disappointing. . . . [*Weltover*] created a risk of lowering the threshold of direct effect in the United States, thereby effectively reducing the circumstances in which a sovereign state may invoke sovereign immunity.").

146. *See, e.g.*, *Voest-Alpine*, 142 F.3d at 897 ("In sum, we hold that a financial loss incurred in the United States by an American plaintiff . . . constitutes a direct effect . . . under the third clause of the commercial activity exception to the FSIA."). Courts adopting the legally significant act requirement seem to suggest that it was intended to require more than a mere financial loss by an American party to trigger the exception. *See supra* note 64 and accompanying text.

147. *See Voest-Alpine*, 142 F.3d at 896 ("*Weltover* simply lowered the standard for finding jurisdiction under the third clause.").

international market has been left without a guide as to what extent parties to transactions can rely on exceptions to immunity under the FSIA.

C. PROTECTING THE STABILITY OF INTERNATIONAL TRANSACTIONS: THE NEED FOR A STANDARD THAT BALANCES COMPETING INTERESTS

Voest-Alpine's departure from the legally significant act requirement in favor of a strict interpretation of the "immediate consequences" test represents more than just a preference for a lower standard for finding jurisdiction under the third clause. The decision ultimately has the potential to affect future commercial transactions between foreign states and American corporations.[148] A lower standard for jurisdiction is protective of American business interests because it provides corporations with a forum in which to secure enforcement a foreign state's contractual obligations.[149] However, in the long run, an extremely low standard may be overprotective, and could potentially damage relations between the United States and foreign governments.

1. Protecting Business Interests

A low standard for granting jurisdiction protects American business interests because it guarantees a fair, adequate remedy for individuals and corporations transacting with foreign sovereigns.[150] If American corporations or individuals are not provided sufficient remedies when dealing with foreign governments, they will be reluctant to enter commercial transactions in the future.[151] An increased risk of loss will raise the costs of dealing with foreign governments and will make international transactions more complicated and less efficient.[152] Corporations involved in overseas transactions will find it necessary to undergo a cost-benefit analysis to weigh the increased costs of associating with a foreign sovereign versus the potential benefits of expanding their operations in the international market.[153]

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148. *See* Donoghue, *supra* note 23, at 521.
149. *See id.*
150. *See id.*; Brockbank, *supra* note 70, at 18.
151. *See* Brockbank, *supra* note 70, at 18.
152. *See id.*
153. *See id.*

Although Congress designed the FSIA to furnish a forum for adjudication of commercial disputes and to provide security in contractual relations, the lack of uniformity among circuit courts applying the Act suggests that it has been unable to provide a sufficient amount of stability in international agreements.[154] The "vague nature of the commercial activity exception" has prevented the development of any consistent case law.[155] Failure to establish definite guidelines for the exception has infused the FSIA with uncertainty and unpredictability.[156] Parties involved in international transactions cannot predict accurately whether nonperformance of their agreements will result in unanticipated, unpredictable, and expensive legal problems.[157] This uncertainty suggests that determinations of jurisdiction under the FSIA should be based on a uniform standard.

By rejecting the "legally significant act" requirement, the *Voest-Alpine* court clearly favored American corporate interests over foreign sovereignty.[158] Yet this decision may not have a desirable effect. Although the court's decision protects American business interests by providing a forum for adjudicating commercial disputes, it may ultimately damage relations with foreign governments.[159] Just as excess grants of immunity may cause American corporations to decrease their participation in the international market, the same chilling effect will logically occur if foreign governments are overly burdened by excess litigation.[160] Thus, adopting such a low standard for jurisdiction may actually work contrary to the court's intent; although it may stabilize international agreements, it may act as a disincentive for foreign sovereigns who do not wish to be dragged into U.S. courts, and may ultimately decrease the amount of international transactions.[161]

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154. *See supra* notes 60-62 and accompanying text.

155. *See* Brockbank, *supra* note 70, at 20.

156. *See supra* notes 60-62 and accompanying text.

157. *See* Ramsey, *supra* note 1, at 76.

158. *See supra* notes 144-47 and accompanying text.

159. *See* Leacock, *supra* note 15, at 121.

160. *See id.*; *cf.* Brockbank, *supra* note 70, at 22 (noting that excess grants of immunity will result in a chilling effect).

161. In contrast to Brockbank, who argues that a chilling effect will result if immunity is granted too often in situations where a sovereign acts in a commercial capacity, this argument focuses on the opposite side of the equation. If U.S. courts follow Brockbank's suggestions and are overly protective of American business interests, foreign governments are more likely to reduce

2. Avoiding the Foreign Policy Risks of Excess Jurisdiction: How a Higher Standard Benefits the International Marketplace

The *Voest-Alpine* decision loses sight of the justifications underlying the FSIA. As a codified theory of restrictive immunity, the FSIA was designed to *balance* the competing interests of American individuals seeking a forum to adjudicate commercial disputes and the sovereign interests of foreign governments.[162] Consequently, the analysis under the commercial activity exception must go beyond protecting American business interests. Courts interpreting the direct effect clause should also consider the interests of foreign governments in being free from excessive litigation and the hindrance of defending the propriety of their acts before foreign courts.[163] Two important considerations should regulate the desire to promote American business interests over those of foreign governments.[164] First, courts should consider their decisions in terms of reciprocity and how exercising jurisdiction will affect the United States as a defendant in foreign courts.[165] Second, courts should be aware of the foreign policy risks of exercising jurisdiction.[166]

By favoring American business interests, *Voest-Alpine* fails to consider either of these factors. As a result, it increases the likelihood that actions against foreign states will have adverse foreign policy consequences.[167] In addition to creating a politically sensitive situation,[168] the real threat of loss and the possibility of litigation raise the costs of international transactions.[169] In order to avoid these costs, foreign governments may opt to forego relations with American entities in favor of less troublesome alternatives, such as making do with their own resources or working with other international companies. This

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their contact with American corporations for fear of being too easily dragged into U.S. courts. *See* Leacock, *supra* note 15, at 121.

162. *See supra* note 36 and accompanying text.

163. *See* Donoghue, *supra* note 23, at 520-21.

164. *See id.* at 521.

165. *See id.*

166. *See id.*

167. *See, e.g.*, Ramsey, *supra* note 1, at 76-77 (noting that application of the commercial activity exception may be problematic in certain circumstances because it might require the judiciary to scrutinize sensitive political situations).

168. *See id.*

169. *See* Brockbank, *supra* note 70, at 22.

shift could have far-reaching consequences for the stability of the foreign marketplace.[170] Although foreign governments would be avoiding the possibility of litigation, the alternatives may be more costly and less efficient.[171] Because "[t]he maximum flow of private foreign capital, trade, and technology is critically important for all countries,"[172] the resulting inefficiencies may lead to a depression in overseas markets.

The legally significant act requirement avoids the problems of a low standard by providing clearer, more favorable standards for foreign governments to assess their relationships with American businesses.[173] Unlike the immediate consequences test, these standards reflect a more measured compromise between the competing interests underlying the policies of the FSIA.[174] The legally significant act requirement promotes sovereignty interests to the extent that it provides a higher standard for granting jurisdiction.[175] Foreign governments can rest assured that the direct effect clause will not be interpreted in a manner that grants jurisdiction over virtually any suit arising out of an international transaction in which an American citizen claims to have suffered a loss from the acts of a foreign state.[176] Furthermore, foreign states are less likely to face the prospect of unanticipated litigation. The legally significant act requirement relies on more consistent standards that are less susceptible to unpredictable judicial interpretation. The benefits of these consistent standards are twofold: foreign governments know what to expect when they enter into commercial transactions, and U.S. courts need not worry about the political ramifications of exercising jurisdiction over sovereign states.

While the legally significant act requirement removes the blanket protection of the immediate consequences test, it will not negatively impact American businesses.[177] In many cases,

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170. *See id.*

171. *See id.*

172. *Id.*

173. *See supra* notes 70-71 and accompanying text.

174. For a discussion of the competing interests underlying the FSIA, see *supra* Part III.C.1.

175. *See supra* notes 70-71 and accompanying text.

176. *See* United World Trade, Inc. v. Mangyshlakneft Oil Prod. Ass'n, 33 F.3d 1232, 1239 (10th Cir. 1994).

177. The legally significant act requirement represents only a slightly higher requirement than the immediate consequences test set forth in *Voest-Alpine*. *See supra* notes 70-71 and accompanying text.

the outcome of the analysis will be the same as the immediate consequences test because international transactions involving American corporations generally involve some legally significant act in the United States.[178] Furthermore, American businesses concerned about the stability of international transactions can try to mitigate the uncertainty by requiring foreign governments to opt out of their immunity by contractual agreement.[179] The FSIA contains a waiver exception that allows parties to contract out of foreign sovereign immunity.[180] While there is no guarantee that a court will enforce a particular agreement,[181] the statutory opt-out provision provides an extra layer of security in international transactions. A well-drafted waiver provision increases the likelihood that a foreign sovereign will be subject to jurisdiction in U.S. courts, effectively eliminating the threat of nonrecourse. Thus, even though the legally significant act requirement may make it slightly more difficult for American individuals and corporations to obtain jurisdiction over foreign governments, parties will still retain the ability to avoid the problems associated with non-enforcement of commercial disputes.

CONCLUSION

Voest-Alpine's rejection of the legally significant act requirement and strict adherence to the immediate consequences test revives the same concerns originally raised by the Supreme Court in *Weltover*. Using the strict language of *Weltover*, it is quite possible that district courts could become small international claims courts. The immediate consequences standard is a significantly easier test for plaintiffs, and is much more skewed towards granting jurisdiction over foreign states rather than preserving sovereign immunity.

As more foreign governments are brought into U.S. courts, this preference for granting jurisdiction may cause a chilling effect on international transactions. Faced with the possibility that U.S. courts will grant jurisdiction in virtually any suit arising out of an international transaction in which an Ameri-

178. *See, e.g.*, Republic of Argentina v. Weltover, Inc., 504 U.S. 607, 618-19 (1992).

179. *See* Brockbank, *supra* note 70, at 21.

180. *See id.* Brockbank suggests that the waiver exception could cure many of the problems associated with the FSIA, but notes that it is rarely invoked. *See id.*

181. *See id.* at 22.

can citizen claims to have suffered a loss, foreign governments may opt to seek less complicated alternatives. Consequently, this shift will reduce the amount of available international opportunities for American businesses and severely limit the overall efficiency of the international market.

The legally significant act requirement presents a viable solution to the problem. Under this formulation, jurisdiction is limited to situations where the effect felt in the United States is a direct result of the foreign state's misconduct. In contrast to the immediate consequences test, this heightened standard better reflects a balance between the competing interests underlying the FSIA. Foreign governments are less likely to reduce their participation with American businesses because the requirement provides predictable results that can be taken into account before an agreement is established. At the same time, American businesses receive nearly the same protection as the immediate consequences test. Overall, the legally significant act requirement promotes stability in international transactions by offering a uniform standard that properly balances the interests of individuals doing business with foreign governments in having their legal rights determined by the courts, and the interest of foreign governments in being free to participate in the international market without undergoing the embarrassment or hindrance of defending the propriety of such participation before foreign courts.