Some Comments on the Interaction of Sovereign Wealth Funds and Sovereign Immunity in Light of a Recent Florida District Court Case: *Capital Trans Int'l v. IPIC et al*.

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There are certain new forms of commercial activities of sovereign States, such as their investments through the so-called sovereign wealth funds ("SWFs"), that are a fairly recent phenomenon. SWFs are government-controlled entities which actively invest in financial markets and enter into diverse commercial transactions. Until a few years ago, it was not common for those financial activities to be deployed by the State or by any of its emanations.

Yet, at the end of 2011, SWFs had nearly US$5 trillion in assets under management[2] (nearly twice the amount controlled by hedge funds).[3] Their role in the world economy became particularly salient in light of the 2007-2008 economic crisis, where certain SWFs from the Middle East and Asia invested multibillionaire amounts of money in US and European financial institutions. For example, the Abu Dhabi Investment Authority ("ADIA"), one of the largest SWFs in the world and the largest in the Middle East,[4] invested US$7.5 Billion in Citigroup.[5] Merril Lynch raised a total of approximately US$10 Billion, initially from Singapore's Temasek and later from similar wealth funds in the Republic of Korea and Kuwait, amongst others.[6] Abu Dhabi's Mubadala (with assets over

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[2] United Nations Conference on Trade and Development, *World Investment Report 2012: Towards a New Generation of Investment Policies*, 13, U.N. Doc. UNCTAD/WIR/2012 (July 5, 2012).

[3] Wouter P.F. Schmit Jongbloed, Lisa Sachs & Karl P. Sauvant, *Sovereign Investment: an Introduction, in* SOVEREIGN INVESTMENT 3, 4 (Wouter P.F. Schmit Jongbloed, et al. eds., 2012).

[4] *Abu Dhabi Investment Authority*, SWF INSTITUTE, http://www.swfinstitute.org/swfs/abu-dhabi-investment-authority/ (last visited May 7, 2014).

[5] Mark Gordon & Sabastian V. Niles, *Sovereign Wealth Funds: an Overview in* SOVEREIGN INVESTMENT 24, 24 (Wouter P.F. Schmit Jongbloed, et al. eds., 2012).

[6] *Id*. at 44.

US$10 Billion) paid US$800 million for control of the Chrysler Building and US$2.35 Billion for 7.5% ownership in the Carlyle Group.[7]

SWFs have clearly become prominent participants in international financial markets. Their transactions and investments transcend continental borders and are no longer the traditional commercial operations that states have ordinarily engaged in for the last 150 years or more. Nevertheless, in the end, SWFs are State-controlled entities. Thus, their financial and commercial activities imply a role for the sovereign immunity of the State.

Not only can SWF dealings with third parties give rise to litigation, but creditors of the parent State can also try to execute their judgments or awards targeting the assets that compose or belong to the SWF. At that point, issues of sovereign immunity will in all likelihood arise. The interaction of SWF activities and sovereign immunity poses certain difficulties that result out of the tension between the dual status of the SWFs as investors in financial markets and State-controlled entities. Indeed, SWFs generally describe themselves as commercial investors pursuing purely financial goals, rather than political objectives.[8] At the same time, where a SWF is involved in litigation, it may tend to invoke sovereign immunity. Also, because they are State-controlled entities, judges may have to apply sovereign immunity rules *sua sponte*.

The recent case of *Capital Trans Int'l v IPIC et al*[9] illustrates some of the most salient issues on the interaction of the sovereign immunity regime under the Foreign Sovereign Immunities Act of 1976 ("FSIA")[10] and SWFs.

In 2010, a Florida Plaintiff, Capital Trans International LLC ("CTI"), filed a breach of contract complaint against three foreign corporate entities: International Petroleum

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[7] Alan M. Rugman, *Sovereign Wealth Funds and Regulation: Some Conceptual Issues in* SOVEREIGN INVESTMENT 297, 300 (Wouter P.F. Schmit Jongbloed, et al. eds., 2012).
[8] INTERNATIONAL FORUM OF SOVEREIGN WEALTH FUNDS, IFSWF MEMBERS' EXPERIENCES IN THE APPLICATION OF THE SANTIAGO PRINCIPLES, 30–31 (July 7, 2011), http://www.ifswf.org/pst/stp070711.pdf.
[9] *Capital Trans Int'l, LLC v. Int'l Petroleum Inv. Co., et al.*, No. 8:10-cv-529-T-30TWG, 2013 WL 557236 (M.D.Fla. Feb. 14, 2013) (order granting motion to dismiss in part).
[10] 28 U.S.C. §1602, *et seq.* (1976).

Investment Company ("IPIC"), Aabar Investments PJSC ("Aabar") and Tasameem Real Estate Company LLC ("Tasameem"). None of them had any office or place of business in Florida. While, from the outset, IPIC was described as a wholly-owned instrumentality of Abu Dhabi, Aabar was referred to as a public joint stock company 75.5% owned by IPIC (the remaining 24.5% owned by the public). Tasameem, on the other hand, was described as a private company with no governmental involvement.

CTI alleged that the US District Court had subject matter jurisdiction over IPIC and Aabar under the FSIA as instrumentalities of a foreign State (Abu Dhabi) that were engaged in commercial activity having a direct effect in the US.[11] IPIC and Aabar objected to the Court having subject matter jurisdiction over them through the FSIA.[12] The Court started off by reviewing the instrumentality status of IPIC and Aabar under §1603 FSIA. IPIC is one of Abu Dhabi's SWFs[13] and it had admitted its status as wholly owned by the Abu Dhabi government. Thus, the Court readily concluded that it met the second prong of §1603(b)(2) FSIA. Indeed, pursuant to §1603(b)(2), 'agency or instrumentality' means any entity which is: i) an organ of a foreign State or political subdivision thereof; or ii) a majority of whose shares or other ownership interest is owned by a foreign State or political subdivision thereof.[14] Naturally, IPIC was a separate legal person (§1603(b)(1) FSIA) and it was neither a citizen of the US nor had it been created under the laws of any third country. That is, it was created under the laws of Abu Dhabi (§1603(b)(3) FSIA). As a result, the Court considered that IPIC met all three 'instrumentality' criteria listed in §1603(b) FSIA.

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[11] CTI did not allege that the Court had jurisdiction over Tasameem through the FSIA.

[12] Defendants moved to dismiss the action based on lack of subject matter jurisdiction, lack of personal jurisdiction, *forum non conveniens,* and failure to state a claim upon which relief could be granted.

[13] *See International Petroleum Investment Company*, SWF INSTITUTE, http://www.swfinstitute.org/swfs/international-petroleum-investment-company/ (last visited May 7, 2014) (the SWF Institute describes IPIC as a Joint Stock Company SWF).

[14] As we shall see below, pursuant to the US Supreme Court in *Dole*, "*[a] corporation is an instrumentality of a foreign state under the FSIA only if the foreign state itself owns a majority of the corporation's shares"*. *Dole Food Co. v. Patrickson*, 538 U.S. 468 (2003). Thus, in order to qualify as 'instrumentality' State direct shareholding is required. However, the *Capital Trans Int'l* District Court did not discuss whether IPIC was directly owned by Abu Dhabi.

Equally, the Court considered that Aabar plainly satisfied the requirements of §1603(b)(1) and (b)(3) FSIA, being a corporation organized under the laws of the United Arab Emirates ("UAE"), not any third country. However, following the US Supreme Court 'direct ownership test' spelled out in *Dole Food Co.*,[15] the District Court determined that, because neither the government of Abu Dhabi nor the UAE directly owned any stock in Aabar, the second prong of §1603(b)(2) could not apply to draw Aabar within the reach of FSIA's instrumentality status.

At the same time, CTI had alleged that, as per §1603(b)(2) FSIA (first prong), Aabar was an instrumentality of the government of Abu Dhabi, being an 'organ' of said government. Confronted with such argument by CTI, the Court regretted the lack of a clear test for determining agency or instrumentality status under the §1603(b)(2) 'organ' prong. In fact, quoting from the case of *USX Corp. v. Adriatic Ins. Co.,* 345 F.3d 190, 209 (3d. Cir.2003), the Court lamented that the FSIA and its legislative history were silent as to a definition of the term 'organ', and that such term is inherently vague and does not have a well-established common law meaning. At the same time, the Court indicated that neither the US Supreme Court nor the Eleventh Circuit had articulated a standard for determining when an entity is an 'organ'. Therefore, the Court looked to other circuit courts for guidance.

The District Court then indicated that four federal circuit courts had addressed the 'organ' prong of §1603(b)(2) FSIA and highlighted that three out of those four courts of appeals had applied identical standards: i) the Second Circuit in *Filler v. Hanvit Bank,* 378 F.3d 213 (2d. Cir.2004); ii) the Ninth Circuit in *EIE Guam Corp. v. Long Term Credit Bank of Japan, Ltd.,* 322 F.3d 635 (9th Cir.2003); and iii) the Fifth Circuit in *Kelly v. Syria Shell Petroleum Dev. B.V.,* 213 F.3d 841 (5th Cir.2000). The Court then emphasized that the 'capstone of organ designation' is whether the entity engages in a public activity on behalf of a foreign government and it took into account that, in order to make such determination, those three circuit courts consider the following five factors:

[15] *Dole Food Co.*, 538 U.S. at 477.

(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.

Subsequently, the *Capital Trans Int'l* Court revealed its disagreement with the fourth court: the Court of Appeals for the Third Circuit in the case of *USX Corp.* which added an additional 'ownership structure of the entity' factor. The *Capital Trans Int'l* Court opined that such additional factor drastically alters the analysis in cases involving tiered corporate ownership and circumvents the reasoning of the US Supreme Court in *Dole Food Co.* which discarded the 'tiering' theory of sovereign immunity. In this connection, the Third Circuit had articulated the additional 'ownership structure of the entity' factor in *USX Corp.* as follows:

> Under the organ prong, as opposed to the majority ownership prong of section 1603(b)(2), a foreign state might own only 10% of an entity; it might own directly 50% of the entity; or it might own even 100% of a holding company that owns 100% of the entity. On the other hand it is possible that a foreign state might not own any portion of any entity that nevertheless is its organ as section 1603(b)(2) does not require a foreign state to have any ownership interest in an entity for it to be its organ. Courts should consider how these different ownership structures might influence the degree to which an entity is performing a function 'on behalf of the foreign government'.[16]

However, the *Capital Trans Int'l* Court stated that adherence to that Third Circuit's extra prong would eviscerate the Supreme Court's careful analysis in *Dole Food Co.* of the Congressional intent behind §1603(b)(2) FSIA. Also, the Court considered that the Third Circuit's view would nullify the particular terms Congress selected in the FSIA, thereby opening the 'organ' prong for all minority held corporations to become instrumentalities when they do not qualify under the 'majority ownership' prong because they are controlled through tiered corporate intermediaries. Thus, the District Court

[16] *USX Corp. v. Adriatic Ins. Co.*, 345 F.3d 190, 209 (2003).

indicated that it would adopt the five-prong test as articulated by the Second, Fifth, and Ninth Circuits.

It is important to note, nevertheless, that neither *Filler v. Hanvit*; *EIE Guam Corp.*; and *Kelly v. Syria Shell*, nor other judgments that have been issued by their respective circuits after *USX Corp.*, have rejected the 'ownership structure of the entity' factor added by the Third Circuit in that judgment.[17] In fact, *Filler v. Hanvit* was issued by the Second Circuit after *USX Corp.* and it did not address the 'ownership structure of the entity' factor. The Court of Appeals for the Ninth Circuit issued *e.g. California v. NRG Energy Inc.*[18] after *EIE Guam Corp.* and, of course, after *USX Corp.* and it did not address the 'ownership structure of the entity' factor either. Likewise, the judgment of the Fifth Circuit in the case of *Board of Regents of University of Texas System v. Nippon Telephone and Telegraph Corp.*,[19] did refer to *USX Corp.* (rendered after *Kelly v. Syria Shell*) but did not disapprove the 'ownership structure of the entity' factor.

In addition, adherence to the Third Circuit's 'ownership structure of the entity' extra factor would not eviscerate in reality the Supreme Court's analysis in *Dole Food Co.* In fact, the 'ownership structure of the entity' factor is just one among five other factors which may serve as guidance to determine whether an entity is an 'organ' under the §1603(b)(2) FSIA first prong. Conversely, the Supreme Court's analysis in *Dole Food Co.* refers to the 'majority ownership' or second prong of §1603(b)(2) FSIA.

Be that as it may, consistent with its approach, the *Capital Trans Int'l* District Court rejected what it called an 'inaccurate equation' by CTI of IPIC with the Abu Dhabi government. It seems like, in the Court's view, CTI had argued, and for purposes of obtaining subject matter jurisdiction over Aabar, that IPIC's ownership of up to 95.3% shareholding in Aabar constituted an indirect acquisition by Abu Dhabi. Yet, the Court

[17] *Id*.
[18] *California v. NRG Energy*, 391 F.3d 1011 (2004) (vacated in part by *Powerex Corp. v. Reliant Energy Services, Inc.*, U.S. 224 (2007)).
[19] *Bd. of Regents of Univ. of Tx. Sys. v. Nippon Tel. and Tel. Corp.,* 478 F.3d 274 (2007).

concluded that IPIC and the Abu Dhabi government were not interchangeable with regards to §1603 FSIA because: "*IPIC does not become a 'foreign state;' rather, IPIC is subsumed within the term 'foreign state' but does not possess the ability to confer instrumentality status on other corporate entities"*.[20]

It appears as though these findings alone would have sufficed for the *Capital Trans Int'l* District Court to stop the enquiry and rule out Aabar's status as an instrumentality of the Abu Dhabi government. Indeed, by rejecting the Third Circuit's 'ownership structure of the entity' factor in *USX Corp.*, the District Court implicitly stated that, in order to qualify as an 'organ' under the first prong of §1603(b)(2) FSIA, there must be direct ownership by the State. Therefore, because Aabar was not directly owned by the government of Abu Dhabi, under the District Court's rationale, it would not have been possible that Aabar qualified as an 'organ', even if it met the five factors identified by the Second, Fifth, and Ninth Circuits. However, on the basis that the jurisdictional challenge was factual instead of facial, the Court delved into an analysis of each of those five factors, subsequently discarding the possibility that each and all of them were fulfilled by Aabar so as to qualify for 'organ' status under §1603(b)(2) (first prong) FSIA.

To require 'direct ownership' so as to satisfy the 'organ' prong of §1603(b)(2) FSIA, seems rather redundant. If that requisite of 'direct ownership' were to apply to every 'organ', then there would be no need for such a separate category of agency or instrumentality. In other words, any 'organ' with separate legal personality that were created under the laws of its parent State as per §1603(b)(1) and (3) would also qualify under the second or 'majority ownership' prong of §1603(b)(2) FSIA. Such result would be contrary to the language of §1603(b)(2) which uses the word 'or' and distinguishes 'organs' from corporate persons a 'majority of whose shares is owned by a foreign State'.

In any case, interestingly enough, in adhering to the five-prong 'organ' test, the Court in the *Capital Trans Int'l* judgment emphasized that the linchpin or capstone of the 'organ'

[20] *Capital Trans Int'l, LLC*, No. 8:10-cv-529-T-30TWG, 2013 WL 557236, at *9 (M.D. Fla. Feb. 14, 2013) (quoting from the Second Circuit in *Filler v. Hanvit Bank,* 378 F.3d 213, 219 (2d Cir. 2004)).

analysis is whether the relevant entity engages in a public activity on behalf of a foreign government. Although in passing, the Court indicated that the key inquiry in order to determine whether an entity qualifies as an 'organ' is whether it serves primarily a private interest, such as profit maximizing, or a public interest, such as industry protection or economic stabilization. This is noteworthy on at least two accounts.

First, the reference to whether an entity serves primarily a private interest as opposed to a public interest, appears to be in line with a 'purpose' test. In other words, The District Court considered it necessary to apply a 'purpose' test in an 'organ' determination, which would in turn serve to decide whether such 'organ' is an 'instrumentality'.

Under the FSIA regime of sovereign immunity, an 'instrumentality' is immune from the jurisdiction of the US courts, subject to the exceptions specified in §§1605 and 1605A FSIA. The US Supreme Court has characterized the 'commercial activity' exception under §1605(a)(2) as the most significant exception to foreign sovereign immunity in the US.[21] §1605(a)(2) FSIA provides for the 'commercial activity' exception to sovereign immunity where the action is based upon: *i)* a 'commercial activity' carried on in the US by the foreign State; or *ii)* an act performed in the US in connection with a 'commercial activity' of the foreign State elsewhere; or *iii)* an act outside the territory of the US in connection with a 'commercial activity' of the foreign State elsewhere that causes a direct effect in the US.

More importantly, pursuant to §1603(d) FSIA, 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'. Therefore, under the District Court reasoning, an 'organ' determination would have to be accomplished on the basis of the 'purpose' that an entity primarily serves. At the same time, such entity could be brought to the Courts of the US under the FSIA as long as – by reference to the 'nature' test – its course of conduct or particular transaction or act is of a commercial character. This result appears paradoxical.

[21] *Republic of Argentina v. Weltover, Inc.,* 504 U.S. 607, 611 (1992).

Secondly, as was previously indicated, the Court referred to 'public interest', mentioning as it did industry protection and economic stabilization as examples. The reference to economic stabilization as a public interest activity is very relevant in a SWF context. Indeed, one of the traditional purposes of SWFs is economic stabilization, and some SWFs have as their exclusive purpose economic stabilization. Thus, the reference to economic stabilization as a public interest activity suggests that the *Capital Trans Int'l* District Court would be readily inclined to characterize an economic stabilization SWF as an 'organ' of the parent foreign State.

In any event, although the Court determined that it lacked subject matter jurisdiction with regard to Aabar, it considered that it possessed subject matter jurisdiction over Defendant SWF IPIC, notwithstanding that it had already been characterized as an 'instrumentality'. Yet, because of CTI's breach of oral contract allegations, the Court determined that the third prong of the commercial activity exception under §1605(a)(2) FSIA was satisfied. It concluded that entering into a contract – albeit elsewhere – is clearly commercial activity and a failure to perform a contractual obligation to pay in the US qualifies as a 'direct effect' under such third prong. Importantly, one notable factor weighed by the Court was that, while CTI alleged that the place of payment was the State of Florida, IPIC did not point to any contradictory evidence about the location of payment.[22]

Nevertheless, that was not the end of the enquiry. The Court, in fact, ended up declining to hear the case on the basis of the *forum non conveniens* doctrine. This doctrine is not the focus of this comment, which is aimed at analyzing the approach taken by the Florida District Court when faced with a case where a SWF and sovereign immunity interacted. However, the dismissal of the *Capital Trans Int'l* case on the basis of the doctrine of *forum non conveniens* brought about an important element for the purposes of IPIC's immunity from execution.

[22] The Court explained that, a declaration by an IPIC officer stating, for example, that IPIC never agreed to make payments in Florida would have sufficed to create a disputed fact.

In fact, in conducting its *forum non conveniens* assessment, the Court considered the likelihood of success of any attempt to enforce an adverse judgment against IPIC in the UAE. At the same time, the Court considered that execution of a judgment issued against another sovereign would be uncertain, as the Court could only attach properties that IPIC owns in the US. Thus, in order to grant IPIC's motion to dismiss on the basis of *forum non conveniens*, the Court required a written stipulation by IPIC consenting to the domestication and execution in the US of any final judgment entered in the UAE. Such stipulation was ordered "*[t]o ameliorate the problem of not receiving enforcement power of a judgment against IPIC in the UAE.*" The case was then dismissed against IPIC based on the doctrine of *forum non conveniens* conditional upon IPIC's written stipulation to domestication and execution in the US of any final judgment.

The requirement of such a stipulation as a condition to dismiss the case on *forum non conveniens* is somehow equivalent to a demand that IPIC waives its immunity from execution in the US. In fact, having been characterized as an 'instrumentality', pursuant to §1609 FSIA, IPIC would be entitled to immunity from attachment and execution in the US. Naturally, IPIC would also be subject to the exceptions contemplated in §1610, including the possibility of a 'waiver.' Nevertheless, the abovementioned condition imposed on IPIC by the *Capital Trans Int'l* Court could cast doubts on the voluntariness of such a 'waiver' from IPIC. That solution may give IPIC some ammunition to resist execution in the US. IPIC could, for example, challenge the validity of the 'waiver'.

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