



Picking the Sovereign's Pocket: Enforcing Your Judgment Against a Recalcitrant Regime

By Michael J. Holland and Ioana Bala



The recent decision of the Supreme Court of Canada in *Kuwait Airways Corporation v. Republic of Iraq and Bombardier Aerospace*¹ raises the question of how to pursue litigation or enforce a judgment

against a state or state agency that claims sovereign immunity from jurisdiction. By the late 1970s, Canada, the United States, and the United Kingdom all had passed statutes incorporating into their laws this public international law principle, along with various exceptions thereto, including an exception pertaining to commercial activity. The commercial activity exception reflects a concern that failing to hold states or state agents accountable in a commercial context would create uncertainty in the marketplace and deter private economic actors from entering into commercial transactions with states. This article examines the *Kuwait Airways* case by providing the factual background and discussing the findings of the Canadian courts with respect to the commercial activity exception. The article further comments on Canadian and U.S. approaches to the doctrine of state immunity and the commercial activity exception. The article concludes with a brief analysis of what can be expected in this type of litigation.

The *Kuwait Airways* Case

The *Kuwait Airways* case arose from the dramatic set of circumstances that gave rise to the Persian Gulf War. The litigation following these events spanned nearly 20 years. Most of the litigation unfolded in the United Kingdom, where Kuwait Airways Corporation (KAC) was awarded large damages. When KAC sought to enforce the judgments it obtained in the United Kingdom, the focus shifted to Canada, largely due to the Canadian presence of Bombardier Aerospace, from which the Republic of Iraq (Iraq) purchased a number of airplanes. KAC petitioned Canadian courts for a seizure order on these airplanes, as well as other Iraqi property located in Quebec.

The litigation at issue concerns the seizure and retention of 10 aircraft, valued at US\$630 million, belonging to KAC from Kuwait International Airport by Iraqi Airways Corporation (IAC) during the Iraqi invasion of Kuwait in 1990. A date crucial for the litigation

is September 17, 1990. As of that date, Iraq purported to dissolve KAC and transfer its assets to IAC.

At the relevant time, IAC was a public statutory body and its property was the private property of the state. While the initial evidence presented suggested that IAC had minimal involvement with the aircraft, subsequent evidence emerged that IAC had been actively involved in appropriating the aircraft after their transfer to Iraqi airfields. IAC had repainted some of the aircraft in its livery, registered and insured the aircraft, and hired engineering staff to prepare the aircraft for flight on commercial routes.

Based on the findings of the U.K. courts, IAC was almost exclusively responsible for the movements of the aircraft subsequent to September 17, 1990. While IAC was subject to supervision by the state, it did not receive any government instructions between September 17, 1990, and January 13, 1991, with the exception of clearance for use of airspace.

History of the U.K. Litigation

The claims brought before the U.K. courts were originally dismissed as against Iraq on the basis of state immunity. The court held that IAC could avail itself of state immunity up to September 17, 1990, because its activities were conducted at the behest of the Iraqi state prior to the decree that purported to vest all of KAC's property in IAC.² Because of allegations of perjury and falsification of documents, however, the court reconsidered these issues. It found that IAC acquired the aircraft on August 9, 1990, and began to prepare them for commercial use forthwith—certainly before the decree of September 17, 1990. Thus, IAC would have no right to immunity for any acts from August 9 forward.³ The court awarded KAC more than US\$1 billion in damages. In addition, the court determined that Iraq, while entitled to state immunity with respect to the claim for damages, was responsible for funding, supervising, and controlling the litigation on behalf of IAC and thus could be responsible for costs of the litigation. Iraq was ordered to pay costs, assessed in the amount of US\$83 million.⁴

Michael Holland is a partner at Condon & Forsyth LLP in New York; he can be reached at mholland@condonlaw.com. Ioana Bala is an associate at Bersenas Jacobsen Chouest Thomson Blackburn LLP in Toronto; she can be reached at ibala@lexcanada.com.

Canadian Decisions

The forum of the litigation moved to Canada shortly after the issuance of the judgment by the English High Court of Justice on July 16, 2008. The courts of Quebec adjudicated two questions: (1) Could the U.K. court's judgment be "automatically" recognized in Quebec? and (2) if not, was there an applicable exception to state immunity? The Quebec Superior Court and Court of Appeal sided with Iraq on both issues.

As the matter worked its way up to the Supreme Court of Canada, there were a number of interesting ancillary legal disputes over the issue of whether aircraft that had been ordered from Bombardier could be detained as security while the issue of enforcement of the U.K. judgment was addressed. There was a factual dispute as to whether Iraq or IAC had ordered the aircraft, but the courts of Quebec ruled that, if it was Iraq, it was not entitled to sovereign immunity in this respect. As a result of these rulings, it appears there will be significant security in the form of undelivered aircraft if KAC ultimately were to prevail.

In the fall of 2010, the Supreme Court of Canada unequivocally overturned both decisions below. The Supreme Court, however, agreed with the courts below on the initial question: the U.K. judgment could not be enforced without regard for the requirements of Canadian legislation.

The Supreme Court of Canada's second crucial finding was that Iraq was not entitled to the protection of state immunity because its activities at issue in this case fell within the commercial exception of the State Immunity Act (SIA).⁵ The Court noted that the SIA not only enshrines the fundamental historical principle of state immunity, but also reflects more recent and more restrictive interpretations of this doctrine. The recent, more restrictive interpretations are intended to reflect "the growing diversity of state functions," including, as in this case, engaging in commercial relations.

The Court also established a test for determining whether a commercial activity exception applies. The Court found that it is not only the *nature* of the act that must be examined, but also its *purpose*. The first inquiry requires an examination of whether the acts at issue could be undertaken by a private person. The Court appears to be of the view that the laws of the United Kingdom and the United States limit the inquiry into the nature of the acts, an issue that we discuss below. The further inquiry into purpose considers the factual context as a whole, beyond the strict categorization of the act itself.

The Court found that Iraq, as the sole proprietor of IAC, controlled and funded IAC's defense throughout the commercial litigation between IAC and KAC. As to the matter in dispute, the Court found that "[t]he original appropriation of the aircraft was a sovereign act, but the subsequent retention and use of the aircraft by IAC were commercial acts."⁶ The subject matter of

the dispute was the retention of the aircraft and not the initial seizure. The Court, therefore, remanded the issue of the recognition of the foreign judgment for reconsideration by the Quebec Superior Court, but without regard to the sovereign immunity principle.

At the time of writing, all other preliminary issues have been resolved and the enforcement proceedings are set to proceed before the Superior Court. Iraq has made a formal undertaking that KAC will receive payment via letters of credit if it is successful in the Canadian proceedings. In an interesting twist, however, Iraq has announced that it is dissolving IAC, which means KAC will have to bring further proceedings to make Iraq pay for the more than US\$1 billion in damages that it obtained in the British courts.

Canadian Law on Sovereign Immunity

The Canadian Supreme Court decision signals that a party seeking to overcome a claim of state immunity in order to enforce a judgment must clear two hurdles: First, even if he or she has obtained a judgment in another jurisdiction and the court in that jurisdiction has ruled that the commercial exception to state immunity applies, a Canadian court will reconsider the matter under Canada's domestic statute before recognizing the judgment. Second, a party bears the burden of successfully arguing that the commercial activity exception applies as interpreted by the Supreme Court in accordance with the Canadian "contextual" approach.

The Supreme Court explained the "contextual" approach in some detail in the seminal case of *Re Canada Labour Code*.⁷ The case concerned an application for certification as a union by a group of civilian Canadian employees of a U.S. military base in the province of Newfoundland. The question before the Court was whether the United States was immune from the jurisdiction of the Canadian Labour Board or whether the commercial exception to state immunity applied. In siding with the United States, the Court rejected the argument that, under the Canadian legislation, it should consider only the nature of the act and not its purpose. The Court explained that simply looking at the nature of the act was not sufficient because it would mean creating rigid categories without taking into account surrounding circumstances. Conversely, examining purpose alone would mean that a state could characterize all of its acts as being for a "sovereign purpose." Thus, the Court commented that, although the U.S. statute on sovereign immunity specifically states that a commercial act must be understood by reference to its nature rather than its purpose, Canadian case law suggests that a combination of nature and purpose should be considered.

In the *Canada Labour Code* case, the Court found that the United States was entitled to immunity from the jurisdiction of the Canadian Labour Board. While a contract of employment was "in and of itself" a

commercial activity, “the management and operation of a military base” was “undoubtedly a sovereign activity.” As such, the application of Canadian labor law might result in disruptions to military operations and make the United States lose control over its military base.⁸

U.S. Law on Sovereign Immunity

Would a U.S. court have reached the same result as the Supreme Court of Canada? We believe the answer is yes.

At first blush, the *Kuwait Airways* case appears to a U.S. practitioner as one that was correctly decided but for the wrong reasons. If there was a valid judgment, there was personal jurisdiction over the defendant and if the defendant had a full hearing, the judgment should be enforced in the courts of the United States under the Uniform Foreign-Country Money Judgments Recognition Act.⁹ This first impression, however, does not withstand scrutiny. Cases decided under the Foreign Sovereign Immunities Act of 1976 (FSIA)¹⁰ indicate that U.S. courts would initiate an analysis similar to that done by the Canadian Supreme Court to determine whether there was sovereign immunity, or any basis for a possible exception thereto under the FSIA. If an exception to sovereign immunity was found, the U.S. court would then look to a domestic statute, such as the Uniform Foreign-Country Money Judgments Recognition Act, to determine whether there was a basis to enforce the foreign judgment. In short, a U.S. court would not have decided this case differently than its Canadian counterpart. The mere fact that there was a foreign judgment entered against Iraq would not automatically entitle that judgment to enforcement in the United States.

While U.S. courts have only rarely adjudicated this issue, an excellent law journal article has addressed the enforcement of court judgments against foreign states and their instrumentalities.¹¹ The article describes the framework for enforcement of foreign court judgments in U.S. courts. First, there must be subject matter jurisdiction, i.e., a waiver of sovereign immunity under FSIA,¹² and then a domestic statute that allows for enforcement of the judgment, such as the Uniform Foreign Money-Judgments Recognition Act or a later version, the Uniform Foreign-Country Money Judgments Recognition Act.

In determining whether to enforce a foreign judgment, the court will first consider whether there is an exception to sovereign immunity. The commercial activity exception in the FSIA holds that

a foreign state shall not be immune from jurisdiction of courts of the United 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 which causes a direct effect in the United States.¹³

The “nexus” requirement in the statute mandates that the foreign state’s commercial acts be tied to the United States and that such commercial acts form the basis of the plaintiff’s cause of action. In *Strategic Technologies PTE, Ltd. v. Republic of China (Taiwan)*,¹⁴ the U.S. District Court for the District of Columbia declined to enforce a foreign judgment entered against Taiwan in Singapore on the grounds that the judgment was not “based upon” commercial activities that satisfied the exception for recognition of the judgment. The parties had entered into an agreement whereby Taiwan had awarded a contract to Strategic Technologies, a Singapore company, to supply an underground test range measuring system. Strategic Technologies sued Taiwan in the High Court of the Republic of Singapore and obtained a judgment in excess of \$1.5 million. The U.S. district court, however, found that Strategic Technologies had not satisfied the FSIA requirement that the commercial activity that provides the jurisdictional nexus be the same activity on which the lawsuit is based.

While the parties agree that a final enforceable judgment existed, there was nevertheless no allegation that the complaint related to Taiwan’s commercial activity connected to the United States. Because plaintiff Strategic Technologies could not satisfy the first step under the FSIA, the court did not need to proceed to the second step, i.e., a domestic U.S. statutory basis for enforcement of a foreign money judgment. Accordingly, the court found that Taiwan was immune from suit in the United States and dismissed the complaint seeking enforcement of the Singapore judgment. This result is entirely consistent with the Canadian Court’s opinion in *Kuwait Airways*.

In another U.S. case, *AF-Cap Inc. v. The Republic of Congo*,¹⁵ the U.S. Court of Appeals for the Fifth Circuit allowed garnishment by a judgment creditor seeking to enforce an English judgment obtained against the Republic of Congo by seizing mining and tax royalties payments located in Texas banks. The court found that the Congo had used these tax and royalty obligations for explicitly commercial purposes and accordingly allowed the garnishment. The court found that using these monies to pay off the Congo’s commercial debts would not shock or disturb the public affairs of the Congo. The court also found that the property was located in the United States, a prerequisite for its attachment. Accordingly, the court found that the tax and royalty obligations were not protected by sovereign immunity and therefore allowed those funds to be used to satisfy the judgment.

The case that is factually closest to *Kuwait Airways* is a recent decision of the U.S. District Court for

the Southern District of New York, *Servaas Inc. v. Republic of Iraq*.¹⁶ *Servaas* filed an action pursuant to New York's Uniform Foreign-Country Money Judgments Recognition Act¹⁷ against the Republic of Iraq seeking recognition of a final money judgment in the amount of \$14,152,800 entered in April 1991 by the Paris Commercial Court in France in favor of *Servaas* and against the Ministry of Industry of the Republic of Iraq. The Republic of Iraq moved to dismiss the complaint, arguing that no exception to sovereign immunity under the FSIA applied. Iraq further contended that the issue of whether Iraq was the same person as the Ministry of Industry for purposes of the court's jurisdiction over Iraq was a question of Iraqi, not U.S., law and, as such, had been decided contrary to plaintiff's assertion that the Ministry of Industry and the Iraqi government were one and the same.

The district court found that the case came within the "commercial activity" exception to sovereign immunity under the FSIA and that the contract, which had been entered into between the plaintiff and the Republic of Iraq or the Ministry of Industry, had a sufficiently "direct effect" in the United States to vest the court with jurisdiction under 28 U.S.C. § 1605(a)(1). The court accepted the plaintiff's argument that the defendant's commercial activities had a direct effect in the United States because all of the machinery, plans, and technologies were delivered to the defendants by *Servaas*, a U.S. company, and that the defendants had failed to pay *Servaas* in the United States pursuant to the terms of the contract. The court rejected the argument that the Ministry of Industry did not enter into the contract on behalf of the Republic of Iraq because the contract required that the Ministry of Industry receive approval from "appropriate governmental authority of Iraq" before the agreement could be finalized. The agreement was in fact finalized and had been approved by the appropriate Iraqi governmental authorities.

The court, having found that the plaintiff satisfied the exception to sovereign immunity under the FSIA, then turned to the question of the enforceability of the French judgment in the United States. New York's Uniform Foreign-Country Money Judgments Recognition Act applies to any foreign country judgment that is final, conclusive, and enforceable where rendered. The only exceptions to enforceability are where the judgment was rendered under a system of law that did not provide impartial tribunals or procedures compatible with the requirements of due process, or where the foreign court did not have personal jurisdiction over the defendant. Iraq conceded that it had been properly served with the proceedings and likewise did not dispute that there was a final judgment of the French court. Accordingly, after the court had conducted its analysis under the FSIA

and the domestic jurisdiction statute for enforcing a judgment (i.e., New York's Uniform Foreign-Country Money Judgments Recognition Act), the court allowed the action to enforce the judgment of the French court to proceed, finding that both tenets (i.e., an exception to sovereign immunity and domestic statutes that allowed the enforceability of the foreign judgment) were met.

While some suggest that the U.S. approach to the commercial activity exception relies on the nature of the act, insofar as the question is whether the act would be undertaken by a private person, U.S. courts also seem to be prepared to go beyond this. Like the Canadian courts, some U.S. courts have adopted a contextual approach. For instance, in the *AF-Cap* case, the court concluded that royalty payments were subject to the commercial exception by applying a "holistic approach" that included a full examination of the uses of the property in the past, present, and future, as opposed to looking at a single instance of commercial use.¹⁸

Conclusion

U.S. and Canadian approaches to the issue of sovereign immunity and the commercial exception are closely aligned. In both jurisdictions, courts will effectively relitigate the issue in accordance with domestic standards on sovereign immunity before moving on to the recognition process. In applying the commercial activity exception, courts in both jurisdictions go beyond a simple categorization of the nature of the act and apply a "contextual" approach that requires examining both the nature and the purpose of an act in combination. Arguably, this is a more state-friendly approach insofar as even if an act is commercial in nature, it may be found to be sovereign by virtue of its purpose. The contextual approach is rather elusive: in the absence of specific facts, it is not possible to predict what will be considered to fall under the commercial activity exception. If the nature of the act is commercial, that will be persuasive. Nevertheless, this may be overturned if the purpose of the act is found to be sovereign. Characterization of the purpose of an act will thus be key in an argument in favor of the commercial activity exception.

If the argument in favor of the commercial activity exception is successful, the next step will be to pursue enforcement proceedings. In the United States, this means determining whether the prerequisites for satisfaction of the foreign judgment (i.e., a final judgment where the defendant had notice and opportunity to appear and there was personal jurisdiction over the defendant) were met. In both jurisdictions, if a domestic statute allows enforcement, a money judgment obtained against a foreign sovereign in a third country may be enforced in local courts.

Endnotes

1. 2010 S.C.C. 40 (Can.).
2. *Kuwait Airways Corp. v. Iraqi Airways Co. et al.*, [1995] 3 All E.R. 694 (U.K.).
3. *Kuwait Airways Corp. v. Iraqi Airways Corp.*, [2003] EWHC 31 (U.K.).
4. *Kuwait Airways Corp. v. Iraqi Airways Co. & The Republic of Iraq*, [2008] EWHC 2039 (U.K.).
5. State Immunity Act, R.S.C. 1985, c. S-18 (Can.).
6. *Kuwait Airways*, 2010 S.C.C. 40, ¶ 35.
7. [1992] 2 S.C.R. 50 (Can.).
8. *Id.* at 79–83.
9. *E.g.*, N.Y. CODE OF PROF'L LEGAL RESPONSIBILITY §§ 5301 *et seq.*
10. 28 U.S.C. § 1602.
11. George K. Foster, *Collecting from Sovereigns: The Current Legal Framework for Enforcing Arbitral Awards and Court Judgments Against States and Their Instrumentalities, and Some Proposals for Its Reform*, 25 ARIZ. J. INT'L & COMP. LAW 665 (2008).
12. Government-owned non-U.S. air carriers are required to waive sovereign immunity as a condition of receiving authorization from the U.S. Department of Transportation (DOT) to serve the United States. DOT Order 2008-9-15 at 2 (DOT authorizations granted to foreign air carriers are subject to a condition that “operations under this authority constitute a waiver of sovereign immunity, for purposes of 28 U.S.C. § 1605(a) . . . with respect to those actions or proceedings instituted against it in any court or other tribunal of the United States that are . . . based on its operations in international air transportation that, according to the contract of carriage, include a point in the United States as a point of origin, point of destination, or agreed stopping place, or for which the contract of carriage was purchased in the United States.”).
13. 28 U.S.C. § 1605(a)(2).
14. Memorandum Op., Civ. Action No. 05-2311 (RMC), May 10, 2007, 2007 WL 1378492 (D.D.C. 2007).
15. 383 F.3d 361 (5th Cir. 2004).
16. 686 F. Supp.2d 346 (S.D.N.Y. 2010).
17. N.Y. CODE OF PROF'L LEGAL RESPONSIBILITY § 5301.
18. *AF-Cap*, 383 F.3d at 369–71.