Global Litigator

PURSUING CLAIMS AGAINST FOREIGN STATE–OWNED COMPANIES LOCATED IN THE UNITED STATES

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A special set of rules applies to lawsuits against companies owned or controlled by a foreign government. These rules arise under the Foreign Sovereign Immunities Act (FSIA), which provides the exclusive basis by which a foreign state or state-owned company can be sued in state and federal courts. Given the significant business conducted by such companies in the United States, all litigators, even those with a more domestic practice, need to be familiar with the FSIA's service requirements and the parameters for and exceptions to sovereign immunity.

A foreign state–owned company—referred to as an "agency or instrumentality" under the FSIA—must be a separate legal entity from the government and must be either majority owned by the foreign state or an "organ" of the foreign state. If a foreign state owns a simple majority stake in the entity, then the company is deemed a state-owned company. The foreign state must hold all its interest *directly*, which means that subsidiaries of a foreign state–owned company are not protected, unless they otherwise qualify as an "organ" of the foreign state.

Organs of a Foreign State

To be an "organ" of a foreign state subject to FSIA protection, the entity must be intertwined with the foreign state. Courts apply a loose list of factors to decide whether the two are sufficiently intertwined, including whether the foreign state created the entity for a national purpose; whether the foreign state actively supervises the entity; whether the state requires the hiring of public employees and pays their salaries; and how the entity is treated under foreign state law.

A "political subdivision" of a foreign state, such as a ministry of justice, is considered to be part of the foreign state itself. By contrast, organs are distinct from the foreign state, although still intertwined. While both are protected to some extent by the FSIA, the assets of an organ, as a separate legal entity, may be seized in some cases where assets of the foreign state are protected. The test for distinguishing an organ from a political

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subdivision focuses on the overall functions of the foreign entity. If the entity serves a governmental function, then courts consider it a political subdivision. If it serves a commercial function, then it may be an organ of the state.

A foreign state–owned company is subject to suit in U.S. courts only if an exception enumerated in 28 U.S.C. § 1605 applies. If no exception applies, sovereign immunity bars the suit. Although the statute lists six possible exceptions, some of them will never apply to foreign state–owned companies because, as commercial enterprises, they do not engage in the same activities as foreign states. Those that most commonly apply to foreign state–owned companies are the commercial activity exception; the waiver exception; the arbitration exception; and the tort exception.

Foreign state–owned companies are not immune from suits involving either their commercial activities carried out in the United States or those that cause a direct effect in the United States. A "commercial activity" is defined as either a regular course of commercial conduct or a particular commercial transaction or act. The question is whether the type of conduct at issue is something in which private parties engage commercially. The purpose behind the activity is not determinative.

For the commercial activity to be carried out in the United States, it must have "substantial contact" with the country. The entire activity need not be performed in the United States, but there must be a sufficient nexus between the plaintiff's cause of action and activities occurring in the United States. It does not suffice that the foreign state–owned company regularly conducts business in the United States that is unrelated to the dispute.

If the commercial activity is not carried out in the United States, then it must have a direct effect in the United States. Courts interpret the phrase "direct effect" to mean an immediate consequence of the defendant's activity, which means there cannot be an intervening act that breaks the chain of causation. Nonpayment is a classic example of conduct that typically satisfies the "direct effect" analysis. If a state-owned company fails to make payments due in the United States under a commercial contract, then the act of nonpayment has a direct effect in the United States. A failure to return property to persons in the United States may have a direct effect as well.

Apart from their commercial activities, foreign state–owned companies are not immune if they explicitly or implicitly waive their immunity. Courts take a cautious approach to this exception and construe waivers narrowly. Explicit waivers are often stated in contracts, and the state-owned company must have been the one to waive immunity.

Implicit waivers are limited to instances in which the foreign company has agreed to arbitrate the dispute in another country, thereby waiving immunity from enforcement proceedings in the United States; has agreed that U.S. law governs a contract; or has filed a responsive pleading in a U.S. court without invoking sovereign immunity. Silence or the mere failure to appear in court after proper service is not considered a waiver.

The implicit waiver exception can be particularly helpful in employment disputes. If a state-owned company signs an employment contract that is governed by U.S. law, then it is not immune from claims brought by the employee in a U.S. court unless some other assertion of immunity is applicable.

Arbitration

Foreign state–owned companies are not immune from actions brought to enforce arbitration agreements. American courts have the power to compel a foreign state–owned company to arbitrate a dispute pursuant to an arbitration agreement. The main question here is whether the arbitration agreement calls for arbitration in the United States or, if arbitration is to take place elsewhere, whether the agreement is governed by the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards.

> State-owned companies remain immune to any claim asserting intentional torts such as malicious prosecution, abuse of process, libel, slander, misrepresentation, deceit, or tortious interference with contract rights.

Courts may also enforce arbitration awards against foreign state–owned companies when the arbitration took place in the United States or when the arbitration was governed by an applicable treaty. The merits of the dispute are not at issue on the question of immunity, meaning a foreign state–owned defendant cannot assert immunity *because* the award is unenforceable. At a later stage in the proceedings, however, the state-owned defendant can attack the validity of the award on the merits.

State-owned companies are not immune from actions for personal injury, death, or property damage. For this exception to apply, both the act and the injury must occur in the United States. State-owned companies retain their immunity

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in two circumstances. First, they retain immunity for the exercise of a "discretionary" function, a term of art for governmental policy decisions. A similar exception applies to claims against the U.S. government under the Federal Tort Claims Act. Second, state-owned companies remain immune to any claim asserting intentional torts such as malicious prosecution, abuse of process, libel, slander, misrepresentation, deceit, or tortious interference with contract rights.

Process Serving

Like all other defendants in U.S. courts, the foreign state–owned defendant must be served with process. In 28 U.S.C. § 1608(b), the FSIA sets forth specific methods of service that must be used. The methods are hierarchical, meaning that a plaintiff cannot skip a method if it is available.

A plaintiff must first attempt to serve process in accordance with any specific arrangement between the parties, such as those set forth in commercial agreements. If there is no such arrangement, then service may be made on any agent of the company authorized to accept service in the United States or in accordance with any applicable treaty on service of process, such as the Hague Convention on Service Abroad of Judicial and Extrajudicial Documents. Finally, if none of those methods is available, service may be effected by letters rogatory; by any form of mail requiring a signed receipt, to be addressed and dispatched by the clerk of the court; or as directed by the court in accordance with the foreign state's law. Service through international mechanisms usually requires translations into the official language of the foreign state.

The due process requirements for personal jurisdiction articulated in *International Shoe Co. v. Washington*, 326 U.S. 310 (1945), and its progeny generally apply to state-owned entities. While sovereign states do not enjoy due process protection, courts have held that foreign state–owned companies must have sufficient minimum contacts with the United States for the courts to have personal jurisdiction. Due process protection is not available, however, for companies that are considered "alter egos" of the foreign state. A company will be considered an alter ego of a foreign state when it is extensively controlled by the state or where recognizing its separateness would work a fraud or injustice.

While foreign state–owned companies enjoy significant immunity in the United States, those protections may not apply when the company acts like a private commercial enterprise.

Extensive control can vary in the eye of the beholder. In *Gater Assets Limited v. AO Moldovagaz*, 2 F.4th 42 (2d Cir. 2021), the district court had ruled that AO Moldovagaz was an alter ego of the Republic of Moldova because it was extensively controlled by the state. The Second Circuit looked deeper into Moldovagaz's corporate structure, the extent of the Republic of Moldova's control over Moldovagaz's prices, and even the voting rights of its board members, to reach the conclusion that Moldovagaz was not an alter ego of the republic.

Attachment

In general, immunity also extends to protect a foreign state–owned company's assets from attachment in U.S. proceedings. However, assets located in the United States that are actively used for a commercial activity may be subject to attachment to enforce a judgment against the company. In certain circumstances, assets that are not actively used by the company may still be subject to attachment if the company itself is engaged in a U.S. commercial activity. Once again, the nature of the activity determines whether it is commercial, not its purpose.

Conclusions

Overall, while foreign state–owned companies enjoy significant immunity in the United States, those protections may not apply when the company acts like a private commercial enterprise. In the global marketplace, many foreign state–owned enterprises are commercial in nature, which means it may be possible to litigate claims against them on the merits. But plaintiffs' counsel must apply the detailed provisions of the FSIA carefully to discern the precise test for the underlying issue. Invoking the wrong standard could doom an otherwise meritorious case. ■

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