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EDITORIAL COMMENTS

UNDERSTANDING THE ACT OF STATE DOCTRINE'S EFFECT

A few years after the *Sabbatino* case¹ was decided, Louis Henkin demonstrated that the act of state doctrine is a federal choice-of-law rule.² He showed that the effect of declining to apply it in any given case is simply to remove it as the controlling choice-of-law rule. In the absence of a statutory directive, the court would then use its normal choice-of-law approach to select the governing law. It might look to international law principles, but only insofar as they are incorporated into federal statutory or common law in the United States, and only if the choice-of-law process selects U.S. law. On the other hand, if the act of state doctrine is applied, its effect is either to choose the foreign law and preempt any escape device, or—essentially the same thing—to preclude the application of United States regulatory law (such as U.S. antitrust law) to conduct that stems from a foreign governmental act.

Judges have not universally recognized Professor Henkin's insights.³ More than 20 years after *Sabbatino* was decided, courts in the United States continue to misunderstand the effect of applying—or of deciding not to apply—the act of state doctrine. Even the U.S. Court of Appeals for the Second Circuit, which hears a disproportionate number of act of state cases, has not always worked deftly with the doctrine. Surprisingly, too, the Department of State's Office of the Legal Adviser still displays an uncertain grasp of the doctrine's effect. This state of affairs was illustrated again in *Chemical Bank II*.⁴

Chemical Bank II arose out of the expropriation of Cuban Electric Co., a Florida corporation that was headquartered and doing its business in Cuba. The expropriation was one of a series directed against U.S. business interests in Cuba. Cuban Electric had outstanding debts to three New York banks, which the Cuban Government did not pay. Either it assumed Cuban Electric's debts and then refused to pay the American creditors, or it as-

¹ *Banco Nacional de Cuba v. Sabbatino*, 376 U.S. 398 (1964).

² See Henkin, *Act of State Today: Recollections in Tranquility*, 6 COLUM. J. TRANSNAT'L L. 175 (1967). As Chief Reporter of the revised *Restatement of Foreign Relations Law*, Professor Henkin has continued to view the act of state doctrine, in most cases, as "a special rule of conflict of laws." RESTATEMENT OF FOREIGN RELATIONS LAW OF THE UNITED STATES (REVISED) [hereinafter RESTATEMENT (REVISED)] §469 Reporters' Note 1 (Tent. Draft No. 7, 1986).

³ Nor have commentators, though they normally pay some deference to him. For a recent critique of the doctrine's choice-of-law explanation, see Chow, *Rethinking the Act of State Doctrine: An Analysis in Terms of Jurisdiction to Prescribe*, 62 WASH. L. REV. 397, 431-35 (1987). Professor Chow gives only passing reference to the essential point that the doctrine is a federal choice-of-law rule, superseding state choice of law even in diversity cases. *Id.* at 434-35 n.251. His preferred rationale, however, is based on principles of legislative jurisdiction and turns out to be basically a choice-of-law approach. *Id.* at 447-74.

⁴ *Banco Nacional de Cuba v. Chemical Bank N.Y. Trust Co.*, 822 F.2d 230 (2d Cir. 1987). *Chemical Bank I* was an earlier appeal in the same case, 658 F.2d 903 (2d Cir. 1981).

sumed only those debts the company owed to non-Americans. The three New York banks also held deposits from some private Cuban banks that were later nationalized. Banco Nacional, as the successor to the private Cuban banks, sued the New York banks to recover the deposits. The New York banks filed setoff counterclaims based on the amounts Cuban Electric had owed them. They claimed, and the court agreed, that the counterclaims were properly asserted against Banco Nacional, since it was the agent or alter ego of the Cuban Government.

Banco Nacional relied on the act of state doctrine in defense to the counterclaims. The Second Circuit's panel treated this not as a choice-of-law issue, but as a question of justiciability. So did the State Department's Legal Adviser, in a Bernstein letter to the court.⁵ In a similar case, another panel of the Second Circuit, having one member in common with the panel on *Chemical Bank II*, had done the same thing.⁶

In both cases, the facts were found indistinguishable from those in the *Citibank* case.⁷ In *Citibank* the Supreme Court held the act of state doctrine inapplicable, even though it could not muster a majority opinion to explain why. Each of these cases involved a Bernstein letter, a counterclaim limited to a setoff and no showing that examination of the Cuban Government's acts would interfere with U.S. foreign relations. The absence of any of these factors probably would have led to the opposite result.⁸

⁵ A Bernstein letter is a letter from the Department of State saying that judicial examination of the foreign government's act in the case at hand would not hamper the conduct of U.S. foreign relations. See *Bernstein v. N.V. Nederlandsche-Amerikaansche Stoomvaart-Maatschappij*, 210 F.2d 375 (2d Cir. 1954). The letter in *Chemical Bank II* disclaimed any interest in having the act of state doctrine applied to the counterclaims, concluding that "the Department of State does not perceive foreign relations difficulties that should bar adjudication of these cases on the merits." The letter also said that the situation "does not compel us to call upon the court to abstain from its normal duty to adjudicate cases properly before it." *Chemical Bank II*, 822 F.2d at 236.

⁶ *Banco Nacional de Cuba v. Chase Manhattan Bank*, 658 F.2d 875 (2d Cir. 1981). The common member was the author of both opinions.

⁷ *First Nat'l City Bank v. Banco Nacional de Cuba*, 406 U.S. 759 (1972).

⁸ A majority of the Justices in *Citibank* rejected the Bernstein letter as a controlling factor, and an even greater majority declined to treat the limited counterclaim as significant. As for the third factor, everyone concedes that the act of state doctrine applies if examination of the foreign government's act, done within its own territory, would demonstrably impede the conduct of foreign relations.

Another possible way around the act of state doctrine might have been to characterize Cuba's repudiation or nonassumption of debts owed to U.S. interests as "private" or "commercial." Cf. *Alfred Dunhill of London, Inc. v. Republic of Cuba*, 425 U.S. 682 (1976). Quite properly, the court in *Chemical Bank II* did not take this route. Cuba clearly made a political decision not to pay U.S. creditors.

It could also have been argued that Cuba had taken property (the claims of the creditors) situated outside Cuba, if the claims had their situs in New York. It is generally thought that the act of state doctrine does not apply to takings of property outside the acting state's territory. See RESTATEMENT (REVISED), *supra* note 2, §469 Reporters' Note 4 (Tent. Draft No. 7, 1986). In fact, though, Cuba did everything it needed to do within its own territory and effectively blocked the creditors' claims. That should satisfy the territorial requirement, regardless of where the debts had their technical "situs."

Another panel of the Second Circuit demonstrated a far superior grasp of the act of state doctrine's effect in the *Lamborn* case.⁹ The doctrine was interposed as a defense to a setoff counterclaim based on a Cuban expropriation, but there was no Bernstein letter. The panel applied the act of state doctrine, treating it as a matter of federal substantive law to be applied on the merits of the case. In effect, though not in so many words, the court used the doctrine to choose Cuban law on the counterclaim.¹⁰ The Cuban expropriation was "nonjusticiable" only in the very limited sense that an act having the effect of law in Cuba was held not subject to judicial reexamination using some other body of law.

Once the court in *Chemical Bank II* had worked its way around the act of state doctrine, it jumped to the conclusion that international law supplied the rule of decision for the counterclaims. It did not stop to examine applicable choice-of-law rules in the forum. Nor did it ask whether federal law in the United States incorporates rules of international law governing the conduct of foreign governments at home. Clearly, it was not applying international law as an international tribunal would. In fact, in purporting to apply international law to the Cuban governmental conduct, it applied a distinctly American brand of international law.

This last point—the likelihood that American judges would apply a parochial version of international law to judge foreign acts of state—may have been at the root of the Supreme Court's unwillingness in *Sabbatino* to engraft an international law exception onto the act of state doctrine.¹¹ In *Chemical Bank II*, the Second Circuit's panel fulfilled that prophecy by looking almost entirely to United States sources for its holding that a state's discriminatory conduct, nullifying the claims of foreign creditors, violates international law.¹²

It is probable that an international tribunal would have reached the same result, despite the paucity of international authority finding a violation solely on the basis of discrimination against foreign nationals.¹³ Thus, the

⁹ *Empresa Cubana Exportadora, Inc. v. Lamborn & Co.*, 652 F.2d 231, 238–39 (2d Cir. 1981).

¹⁰ *Cf. Ricaud v. American Metal Co.*, 246 U.S. 304, 309 (1918) (in an act of state case, the action of the foreign government "must be accepted by our courts as a rule for their decision").

¹¹ See 376 U.S. at 433 (where the Supreme Court majority revealed a certain skepticism regarding lower courts' ability in future cases to handle less clear violations of international law than occurred in *Sabbatino* itself).

¹² The court relied heavily on the *Restatement (Second)* and the *Restatement of Foreign Relations Law (Revised)*. Both *Restatements* disclaim a parochial point of view, saying that they represent "the opinion of The American Law Institute as to the rules that an international tribunal would apply if charged with deciding a controversy in accordance with international law." RESTATEMENT (REVISED), *supra* note 2, *Introduction* (Tent. Draft No. 5, 1984) (quoting RESTATEMENT (SECOND)). But as anyone who attended the ALI debates on the revised *Restatement* knows, the Institute's opinion is shaped by the views and interests of its (American) members.

The court in *Chemical Bank II* cited only two non-American sources: a British scholar (B. A. Wortley) and a 1931 arbitral award by the Mexican-U.S. General Claims Commission. The point in the arbitral award on which the court relied was actually a quotation from an American textbook, 1 J. SUTHERLAND, *LAW OF DAMAGES* 126 (4th ed. 1916). See *Dickson Car Wheel Co. v. United Mexican States*, 4 R. Int'l Arb. Awards 669, 681 (1931).

¹³ Recent arbitral awards that have considered assertions of discriminatory taking or breach of contract have found additional grounds for holding the governmental acts unlawful, or have

point is not that the American court reached the wrong conclusion, but that in reaching its conclusion it applied an Americanized version of international law to the acts of a foreign government, without recognizing that it had engaged in a choice-of-law process or that its application of the chosen law was parochial.

When an American court applies U.S. law to the foreign acts of a foreign government, and when that U.S. law has a strong regulatory character, a jurisdiction-to-prescribe issue is presented. This, too, the panel in *Chemical Bank II* failed to perceive. As in transnational antitrust cases, the court is fashioning a remedy for conduct abroad by a non-U.S. national that is not countenanced by U.S. standards. When the conduct is by a foreign government rather than by a private cartel, the issue is all the more sensitive.¹⁴

As it did on the issue of discrimination, the panel in *Chemical Bank II* may well have stumbled its way to a justifiable result on this point. This is primarily because—as noted above—its conclusion on discrimination probably would have been reached also by an international tribunal. The legitimacy of a foreign government's complaint about the reach of U.S. prescriptive jurisdiction is diluted, though not entirely eliminated, if the rule prescribed is no more stringent than one an international tribunal would prescribe. Arguably, the panel's result might also be supported by the rationale of objective territoriality often used in international antitrust cases, since the effects of the Cuban action were foreseeably felt by the banks in the United States. This rationale, though, has its own parochial credentials.¹⁵

Not only should U.S. courts, in applying or declining to apply the act of state doctrine, reach justifiable results; they should know how they got there and they should take a justifiable route to get there. The panel in *Chemical Bank II* was lucky; it reached a justifiable conclusion without betraying much awareness of how to go about it. Other courts may not be so lucky in close cases.¹⁶

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failed to find that there actually was discrimination against foreign nationals. See *BP Exploration Co. (Libya) Ltd. v. Libyan Arab Republic*, 53 ILR 297, 329 (1979); *Libyan American Oil Co. v. Libyan Arab Republic*, 20 ILM 1 (1981); *Kuwait v. American Independent Oil Co.*, 21 ILM 976 (1982); *American International Group, Inc. v. Iran*, 4 IRAN-U.S. CLAIMS TRIBUNAL REP. 96 (1983), 23 ILM 1 (1984); *Liberian Eastern Timber Corp. v. Liberia*, 26 ILM 647 (1987). Cf. Schachter, *International Law in Theory and Practice*, 178 RECUEIL DES COURS 9, 314-21 (1982 V).

Of course, the Cuban discrimination in *Chemical Bank II* was in the form of an uncompensated deprivation of rights. Thus, the court did not have to rely solely on discrimination to find an international law violation, but it did so nevertheless.

¹⁴ This point is more fully developed in Kirgis, *Act of State Exceptions and Choice of Law*, 44 U. COLO. L. REV. 173, 182-85 (1972), and *Addendum*, *id.* at 379, 380-85 (1973). Cf. Chow, *supra* note 3, at 447-74.

¹⁵ See RESTATEMENT (REVISED), *supra* note 2, §402 comment *d* and Reporters' Note 2 (Tent. Draft No. 6, 1985).

¹⁶ The approach outlined in this Comment should be applied even in a case involving the Second Hickenlooper Amendment. The amendment, 22 U.S.C. §2370(e)(2) (1982), contains its own choice of (U.S.) law but should be interpreted to apply only when a claim of title or other right to property stems from a violation of "true" international law—not just of standards asserted by the United States Government. See Kirgis, *supra* note 14, at 181-82, 185-86.