

EXCHANGE CONTROL: ACT OF STATE, PUBLIC POLICY, THE IMF'S ARTICLES OF AGREEMENT, AND OTHER COMPLICATIONS

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I. INTRODUCTION

Patria, a member of the International Monetary Fund (Fund)¹, provides by law that all obligations of its residents to make payments are to be discharged in the domestic currency whatever may be the contractual currency of account or of payment and whether the payee is or is not a resident in Patria's territory. Patria provides that the domestic currency is the exclusive currency of payment. That expression is used here so as to avoid *a priori* solutions that may seem to follow from the use of such terminology as legal tender, *cours légal*, and *cours forcé*. Legal tender or *cours légal* is defined as the currency that creditors are required by a sovereign legislator to accept in discharge of indebtedness owed to them and also as the means of circulation (notes, coins) that must be accepted in accordance with such a provision of law. *Cours forcé* is defined as the means of circulation that are legal tender and are made irredeemable by the monetary authorities issuing the currency.

Nothing is said in these definitions about the negation of any right of debtors to contract and settle indebtedness in a currency foreign to the sovereign. Some problems of monetary law are not problems to be settled by invoking definitions of legal tender and associated concepts, because the problems relate to situations that are not wholly domestic, and have therefore entered the terrain of exchange control.² The problems are then within the field of interest of the Fund.

Prescription of the exclusive currency of payment is not the only

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1. Articles of Agreement of the International Monetary Fund, Apr. 30, 1976, 29 U.S.T. 2203, T.I.A.S. No. 8937 [hereinafter cited as Articles of Agreement].

2. See 2 J. GOLD, THE FUND AGREEMENT IN THE COURTS 46, 48, 62, 78-79, 117 (1982) [hereinafter cited as 2 J. GOLD]; F. MANN, THE LEGAL ASPECT OF MONEY: WITH SPECIAL REFERENCE TO COMPARATIVE PRIVATE AND PUBLIC INTERNATIONAL LAW 41-42, 74-76, 162-66, 186, 266-67, 322 (4th ed. 1982); A. NUSSBAUM, MONEY IN THE LAW, NATIONAL AND INTERNATIONAL: A COMPARATIVE STUDY IN THE BORDERLINE OF LAW AND ECONOMICS 46, 56, 268, 269, 346 (1950).

form of exchange control available to a sovereign. The legislator may provide, for example, not that nonresident creditors must accept the domestic currency of the legislator, but that they have an option to accept it in lieu of the contractual currency of payment. Another possible variant is suspension of the discharge of obligations payable in foreign currency until a license is granted, without provision for payment in some other form.

Exchange control, which may or may not be in the form of a regulation that the domestic currency is the sole currency of payment (prescription of the exclusive currency), will be discussed under the headings of *The Fund's Articles, Act of State Doctrine, Some U.S. Cases Involving the Doctrine and Exchange Control, and Some Interrelationships Among Act of State, Public Policy, and the Fund's Articles.*

A. *The Fund's Articles*

Prescription of the exclusive currency is not in itself a restriction on the making of payments and transfers for current international transactions within the meaning of either Article VIII, Section 2(a)³ or the transitional arrangements of Article XIV, Section 2⁴ of the Fund's Articles. The Supreme Court of New York noted the distinction between prescription and restriction in *De Sayve v. de la Valdene*.⁵ The court concluded that under French law, the defendant, who had undertaken obligations to pay U.S. dollars and British pounds, was required, in the circumstances of the case, to discharge his obligations in French francs. The parties were French citizens, and the obligations were signed and delivered in France, but it was not stated where payment was to be made. Nor did it appear that either party had become a nonresident of France. The court noted the concession by the defendant that this provision of French law was not an exchange control law that was enforceable under the Articles

3. "Subject to the provisions of Article VII, Section 3(b) and Article XIV, Section 2, no member shall, without the approval of the Fund, impose restrictions on the making of payments and transfers for current international transaction." Articles of Agreement, *supra* note 1.

4. "A member that has notified the Fund that it intends to avail itself of transitional arrangements under this provision may, notwithstanding the provisions of any other articles of this agreement, maintain and adapt to changing circumstances the restrictions on payments and transfers for current international transactions that were in effect on the date on which it became a member. Members shall, however, have continuous regard in their foreign exchange policies to the purposes of the Fund, and, as soon as conditions permit, they shall take all possible measures to develop such commercial and financial arrangements with other members as will facilitate international payments and the promotion of a stable system of exchange rates. In particular, members shall withdraw restrictions maintained under this Section as soon as they are satisfied that they will be able, in the absence of such restrictions, to settle their balance of payments in a manner which will not unduly encumber their access to the general resources of the Fund." *Id.*

5. 124 N.Y.S.2d 143 (1953).

of the Fund. The court probably meant by this statement that the obligations were not unenforceable under Article VIII, Section 2(b).⁶ The court held that the provision of French law was not a penal or revenue law, which the courts of another country will not enforce. The provision was an expression of French public policy, but the court found it unnecessary to decide whether for this reason the provision would not be enforced, although the court leaned to that view. The defendant had conceded that it would make no difference whether or not his obligation was measured in French francs if the court were to adopt the technique for translation that in fact the court did favor. The technique would be, first, to translate the foreign currencies into French francs at the rate of exchange prevailing at the dates when the obligations should have been discharged and, then, for the purpose of judgment, to translate the francs into U.S. dollars at the same rates. The effect would be equivalent to awarding the dollar amounts without going through these stages, together with the dollar equivalent of the sterling amounts.

A court in Patria will apply Patria's prescription of the exclusive currency, but the question is whether courts in other countries will recognize the prescription. These courts may find the answer to the question in Article VIII, Section 2(b) of the Fund's Articles if exchange control is involved or, alternatively, in their traditional private international law if that provision of the Articles does not apply or if exchange control is not involved.

If a member's practice constitutes a restriction within the meaning of the Fund's definition and is authorized by the Articles or approved by the Fund, Article VIII, Section 2(b) may be applicable. Three elements in this statement will be examined in turn: practice, definition, and consistency with the Articles. Article VIII, Section 2(b) may apply in circumstances, and may establish conditions, other than those that will be examined, but these other circumstances and conditions are beyond the scope of the present discussion.

The first of the three elements to be examined is a member's practice. Although, as noted above, the prescription by law of an exclusive currency is not automatically a restriction on payments and transfers within the meaning of the Articles, the prescription can take on this character in some circumstances. The Fund's conclusion that there is such a restriction depends on a member's behavior and not on the exist-

6. "Exchange contracts which involve the currency of any member and which are contrary to the exchange control regulations of that member maintained or imposed consistently with this Agreement shall be unenforceable in the territories of any member. In addition, members may, by mutual accord, cooperate in measures for the purpose of making the exchange control regulations of either member more effective, provided that such measures and regulations are consistent with this Agreement." Articles of Agreement, *supra* note 1.

ence of legal provisions. If a member has a provision on its statute books under which payments could be, but are not, restricted, the Fund will hold that the member is not maintaining or imposing a restriction. The converse is also true: the Fund may find that a restriction exists even though there is no provision of law that authorizes the practice. For example, undue delay in authorizing payments (or in providing foreign exchange by the instrumentality of the government that makes exchange available if payments in foreign currency are permitted) may constitute a restriction even though there is no formulated direction requiring the delay. On payments arrears, the Fund has decided that:

Undue delays in the availability or use of exchange for current international transactions that result from a governmental limitation give rise to payments arrears and are payments restrictions under Article VIII, Section 2(a), and Article XIV, Section 2. The limitation may be formalized, as for instance compulsory waiting periods for exchange, or *informal or ad hoc*.⁷ [emphasis added]

Another consequence of applying the test of actual restrictiveness is that if a member has adopted a legal provision under which a restriction is applied, and then abandons the restriction but retains the provision, the revival of the restrictive practice must be considered the introduction of a restriction. Approval is required under Article VIII, Section 2(a) whether or not the member is availing itself of the transitional arrangements of Article XIV.⁸

The prescription of an exclusive currency may be a restriction if a member's practice is within the Fund's definition of a restriction:

The guiding principle in ascertaining whether a measure is a restriction on payments and transfers for current transactions under Article VIII, Section 2, is whether it involves a direct governmental limitation on the availability or use of exchange as such.⁹

The adjective "international" after the word "current" must be understood to have been intended. Undue delay in authorizing payments is only one example of conduct that may be covered by this definition of restrictions. The definition does not refer to restrictions on capital trans-

7. INTERNATIONAL MONETARY FUND, SELECTED DECISIONS AND SELECTED DOCUMENTS 244 (10th issue 1983) [hereinafter cited as SELECTED DECISIONS].

8. 1 J. HORSEFIELD, THE INTERNATIONAL MONETARY FUND 1945-1965: TWENTY YEARS OF INTERNATIONAL MONETARY COOPERATION 248-50 (1969); S.1679-86, 98th Cong., 2d Sess., 130 CONG. REC. (daily ed. Feb. 27, 1984) (Memorandum: The Application of International Law to Iranian Foreign Exchange Regulations).

9. SELECTED DECISIONS, *supra* note 7, at 241-42.

fers, but the same test would be applied, with the substitution of capital transfers for the payments and transfers that are referred to.

The third element to be considered is consistency with the Articles. *Prima facie*, the prohibition of payments by residents to nonresidents in currencies other than Patria's is a restriction within the meaning of Article VIII, Section 2(a) and Article XIV, Section 2 when it applies to current transactions. The prohibition falls, *prima facie*, within the one provision or the other.

The two provisions, however, refer to "payments and transfers." If a nonresident contracting party must accept payment in Patria's currency under the law that Patria observes or the practice it follows, but the payee can exchange the currency for his own currency, or for some other currency with which he can get his own currency, the conclusion, subject to certain qualifications discussed below, is that Patria is not restricting "payments and transfers," because it is not restricting transfers.

It must be noted that the two provisions relate to current international transactions. Therefore, the nonresident payee must have received the proceeds as the result of a current international transaction as defined by Article XXX(d).¹⁰ Moreover, the proceeds must be the result of a current international transaction that took place recently. If the nonresident payee has allowed the proceeds to remain in Patria for more than the period implicit in the concept of a recent transaction as understood by the Fund, the proceeds become capital. If the proceeds have become capital, Patria can restrict them under Article VI, Section 3 without the need for approval by the Fund. Patria is not allowed, however, to delay unduly the payee's exchange (i.e., transfer) of the proceeds. If Patria were able to impede an exchange that the nonresident payee wanted to make, transfer by the payee might be frustrated, because Patria would be able to restrict transfer of the proceeds as a movement of capital. This analysis follows from the reference to undue delay in Article VI, Section 3:

Members may exercise such controls as are necessary to regulate international capital movements, but no member may exer-

10. "Payments for current transactions means payments which are not for the purpose of transferring capital, and includes, without limitation:

- (1) all payments due in connection with foreign trade, other current business, including services, and normal short-term banking and credit facilities;
- (2) payments due as interest on loans and as net income from other investments;
- (3) payments of moderate amount for amortization of loans or for depreciation of direct investments; and
- (4) moderate remittances for family living expenses.

The Fund may, after consultation with the members concerned, determine whether certain specific transactions are to be considered current transactions or capital transactions." Articles of Agreement, *supra* note 1.

cise these controls in a manner which will restrict payments for current transactions or which will unduly delay transfers of funds in settlement of commitments, except as provided in Article VII, Section 3(b) and in Article XIV, Section 2.¹¹

The analysis of the relationship between the prescription of the exclusive currency of payment and restrictions on payments and transfers for current international transactions is derived from the purpose of the Fund that refers to a multilateral system of payments for such transactions:

To assist in the establishment of a multilateral system of payments in respect of current transactions between members and in the elimination of foreign exchange restrictions which hamper the growth of world trade.¹²

Freedom for transfers is essential for the effectiveness of the multilateral system of payments and transfers for current international transactions. That system is not promoted if the proceeds of current international transactions are locked up in blocked accounts in Patria or if payees are permitted to use the proceeds only for investment in Patria or only for payments for current transactions with residents of that country.

The multilateral system of payments means a system in which contracting parties can make payments freely to the residents of all member countries. A resident of Terra may demand payment in a particular currency, and indeed the monetary authorities of Terra may provide that he is to receive payment in a particular currency, whether Terra's or some other currency. If Terra prescribes the currency of receipt for its resident payees, Terra is deemed not to be imposing a restriction within the meaning of the Articles. The effect of the language of Article VIII, Section 2(a) in referring to restrictions on the "making" of payments and transfers is that prescription of the currency of receipt by residents is not a restriction. The objective of this usage is to prohibit the monetary authorities of the payor's country of residence (Patria) from restricting the payor's ability to obtain whatever currency he needs for making the payment demanded by the payee in Terra. The payee resident in Terra or the monetary authorities of that country are allowed to prescribe the currency of receipt, if they wish, because a large proportion of the world's payments for trade and other current account transactions is made in a relatively small number of currencies.

11. *Id.* The reference to Article VII, Section 3(b), the so-called scarce currency clause, can be ignored, because no action has been taken under the provision throughout the history of the Fund.

12. Articles of Agreement, *supra* note 1, at art. I ¶ (iv).

The duty incumbent on the monetary authorities of Patria is not to restrict payments by their resident payors to payees resident in other countries, including Terra, or transfers of the proceeds by the payees to their own countries. If Patria has instructed its resident payors to make these payments only in Patria's currency, the instruction cannot be justified as a mere exercise of Patria's right to determine the currency that is to be legal tender, even if the payments to nonresident payees are made in Patria's territory. The measure will be a restriction under the Articles unless the payee is free to exchange, directly or indirectly, the proceeds he receives in Patria's currency for his own currency. When he receives his own currency, he can turn to his own monetary authorities, or go into the exchange market within his country, and purchase, with his currency, whatever currency he needs for entering into a current international transaction with the residents of any other member country. A multilateral system of payments is promoted because the resident of Terra will be able to take home, in the form of his own currency, his proceeds as payee in a transaction with a resident of Patria, and then use the proceeds to obtain whatever currency he needs as a payor in a transaction with a resident of a third country.

If Patria interferes with the ability of the resident of Terra to transfer the proceeds of his current international transaction, Patria must obtain the Fund's approval for the restriction under Article VIII, Section 2(a) unless the restriction is authorized by the Articles under Article XIV, Section 2 as part of the transitional arrangements. If Patria introduces the prescription of an exclusive currency of international payment, Patria will probably also introduce a restriction on transfers of the proceeds by nonresident payees. Nonresidents, aware that they will be unable to make transfers, are likely to refrain from entering into new contracts with residents of Patria. The legal problems that are litigated in courts outside Patria usually involve the effect of the restriction on contracts entered into before Patria acted. Patria will apply the restriction to these contracts because of the necessity to prevent further losses of monetary reserves in what has become a serious economic situation. For foreign courts to hold that Article VIII, Section 2(b) does not apply to a restriction insofar as it has been imposed on existing contracts is tantamount to insistence on a further hemorrhage before the flow of blood can be staunched. The problem that has induced a member to impose exchange control may be capital outflow. Foreign courts should not require the outflow to continue. Nothing in the language or economic logic of Article VIII, Section 2(b) authorizes a distinction between contracts on the basis of the date at which they have been entered into. The distinction is not so embedded in law as to justify the proposition

that supervening changes in circumstances, even in the law itself, must be treated as irrelevant.

If the defendant relies on Article VIII, Section 2(b) because of a provision of Patria's law that imposes a restriction according to the foregoing analysis, the conditions of Article VIII, Section 2(b) must be satisfied. One condition is that the exchange control regulation under which Patria applies the restriction is maintained or imposed consistently with the Articles. If the restriction is on payments and transfers for current international transactions, the approval of the Fund is necessary under Article VIII, Section 2(a). If the restriction has been maintained since Patria joined the Fund, either in the original form of the restriction or with no more than the adaptation of it to changing circumstances, and if Patria is availing itself of the transitional arrangements of Article XIV, Section 2, the restriction is authorized by the Articles without the necessity for approval by the Fund. The restriction is authorized so as to allow the member to determine when to make its currency fully convertible for current international transactions in accordance with Article VIII. If the restriction is not on the proceeds of a recent current international transaction but on the transfer of capital, the restriction will be authorized by Article VI, Section 3. A restriction of that character is authorized so as to enable the member to defend itself against the destabilization of its economy by inflows or outflows of capital.

It is necessary now to consider exchange rates. Suppose that Patria permits a nonresident payee to exchange the proceeds of a recent current international transaction¹³ for his own currency at a rate of exchange that is unfavorable to him compared with the rate of exchange that can be obtained in other exchange transactions.¹³ If, as is likely, the unfavorable exchange rate is a multiple currency practice,¹⁴ the Fund's approval of the practice is necessary under Article VIII, Section 3.¹⁵ Moreover, the multiple currency practice will be a restriction under Article VIII, Sec-

13. See Zamora, *Peso-Dollar Economics and the Imposition of Foreign Exchange Controls in Mexico*, 32 AM. J. COMP. L. 99 (1984). For other techniques, based on the consent of payees, to alleviate economic distress, see Lieseca & Studwell, *Latin American Accounts Receivable: To Sue for Collection or to Refinance?*, 39 BUS. LAW. 495 (1984).

14. SELECTED DECISIONS, *supra* note 7, at 257-59; J. GOLD, SDRS, CURRENCIES, AND GOLD: SIXTH SURVEY OF NEW LEGAL DEVELOPMENTS 22-27 (IMF Pamphlet Series No. 40, 1983) [hereinafter cited as GOLD, Pamphlet No. 40].

15. "No member shall engage in, or permit any of its fiscal agencies referred to in Article V, Section 1 to engage in, any discriminatory currency arrangements or multiple currency practices, whether within or outside margins under Article IV or prescribed by or under Schedule C, except as authorized under this Agreement or approved by the Fund. If such arrangements and practices are engaged in at the date when this Agreement enters into force, the member concerned shall consult with the Fund as to their progressive removal unless they are maintained or imposed under Article XIV, Section 2, in which case the provisions of Section 3 of that Article shall apply." Articles of Agreement, *supra* note 1.

tion 2(a) as well, but approval under Section 3 will be taken to be approval under Section 2(a) also.

If Patria is availing itself of the transitional arrangements and was enforcing the multiple currency practice when Patria entered the Fund, the restriction is authorized by Article XIV, Section 2. If the practice is imposed at a later date, or even if it was in force when Patria entered the Fund but is being adapted, Patria must obtain approval under Article VIII, Section 3. If the practice was in force when Patria entered the Fund, but Patria is now undertaking to perform the obligations set forth in Article VIII, Sections 2, 3, and 4, the practice is authorized by the Articles but Patria must consult with the Fund on the progressive removal of the practice. The Fund enforces the member's obligation of progressive removal by approving the practice for the time being.

A special problem may arise if the multiple currency practice is confined to capital transfers. The Fund has not decided whether a member is free to adopt the practice under Article VI, Section 3 because the practice is a restriction on capital transfers, or whether the member must obtain the approval of the Fund under Article VIII, Section 3 because the measure is a multiple currency practice. The problem may be less acute because members may find it difficult to segregate capital transfers from payments and transfers for current international transactions as defined by the Articles. If the segregation is not complete, the Fund's approval is unquestionably necessary for the multiple currency practice to the extent that it applies to the payments and transfers for current international transactions. If the Fund grants approval for these payments and transfers, the practice should be deemed to be consistent with the Articles for all the payments and transfers to which the practice applies.¹⁶ If the member is able to confine the practice to capital transfers, and the Fund has not reacted to it, the member should not be prejudiced by the Fund's irresolution. The practice should be deemed to be consistent with the Articles.

The defendant may raise the defense that Patria's exchange control regulations prohibit transfers except at the special rate of exchange approved by the Fund as a multiple currency practice. The defendant would argue that a foreign court that did not recognize the special rate would be acting contrary to Article VIII, Section 2(b). A successful defense is harsh treatment of the plaintiff, but the effect of a regulation forbidding transfers is also harsh treatment if the regulation is approved by the Fund or authorized by the Articles. The justification of the result

16. GOLD, Pamphlet No. 40, *supra* note 14, at 33-34.

in both cases would be that the public interest predominated over the plaintiff's interest.

The plaintiff may respond that the defense of Article VIII, Section 2(b) to a claim that rejects the multiple currency practice rests on the mistaken assumption that Article VIII, Section 2(b) requires the enforcement of contracts in accordance with Patria's regulations. The provision deals only with the unenforceability of contracts. Patria's law does not prohibit performance in decreeing an unfavorable exchange rate for performance. If the court were to accept this response, the court would conclude that Article VIII, Section 2(b) was not relevant. The court would have to find the appropriate rate of exchange, and might still apply the special rate according to some principle of the *lex fori*.

B. Act of State Doctrine in the United States

Exchange control is an aspect of a state's power to manage its currency, although subject now to the international obligations that have been accepted by the state. "Control of the national currency and of foreign exchange is a necessary attribute of sovereignty."¹⁷ Viewed in this way, the imposition of exchange control can be considered an action within the Act of State doctrine, provided that the necessary conditions for the application of the doctrine are satisfied.¹⁸ It is not easy to define exchange control or to distinguish it from some other governmental actions to which the Act of State doctrine can apply. Against the background of the Fund's Articles, a country's exchange control can be described as the governmental control of payments and transfers that affect the country's balance of payments, or as the governmental control of the means used to make, or of the means resulting from, such pay-

17. *Naamloze Venootschap Suiker-Fabriek v. Chase Nat'l Bank of New York*, 111 F. Supp. 833, 845 (S.D.N.Y. 1953).

18. An extraordinary amount of attention has been devoted to the Act of State doctrine in recent articles. See, for example, Conant, *The Act of State Doctrine and Its Exceptions: An Introduction*, 12 VAND. J. TRANSN'L L. 259 (1979); Cooper, *The Act of State Doctrine: Ethiopian Spice v. Kalamazoo Spice*, 12 DEN. J. INT'L L. & POL'Y 285 (1983) [hereinafter cited as Cooper, *Act of State*]; Corcoran, *IAM v. OPEC: Commercial Activity: One Factor in a Balancing Approach to the Act of State Doctrine*, 14 LAW & POL'Y INT'L BUS. 215 (1982); Kahale, *Characterizing Nationalizations for Purposes of the Foreign Sovereign Immunities Act and the Act of State Doctrine*, 6 FORDHAM INT'L L.J. 391 (1982-83); Kamli, *The Act of State Doctrine and U.S. Antitrust Law*, 12 LAW & POL'Y INT'L BUS. 503 (1980); Krane, *Rehabilitation and Exoneration of the Act of State Doctrine*, 12 N.Y.U. J. INT'L L. & POL. 599 (1980); Lindskog, *Act of State or Act of Desperation?*, INT'L FIN. L. REV., Dec. 1983, at 4; Mathias, *Restructuring the Act of State Doctrine: A Blueprint for Legislative Reform*, 12 LAW & POL'Y INT'L BUS. 369 (1980); Rendell, *United States Restatement of Rules of International Law*, INT'L FIN. L. REV., Feb. 1984, at 20; Silverman, *Act of State Doctrine: Determining its Viability in a Suit Involving an Expropriation by Cuba of Foreign-Owned Assets*, 14 LAW. AMERICAS 337 (1982); Zimmerman, *Applying an Amorphous Doctrine Wisely: The Viability of the Act of State Doctrine after the Foreign Sovereign Immunities Act*, 18 TEX. INT'L L.J. 547 (1983) [hereinafter cited as Zimmerman, *Amorphous Doctrine*].

ments and transfers. Governmental in this context includes the actions of central banks even when they are independent of governmental direction.

Judicial pronouncements sometimes add the motive of defense of the country's balance of payments, or defense of the currency, when the country is in economic difficulty, but the Fund does not consider this element essential in its view of exchange control. A government may have another motive or mixed motives for exchange control. Even the defense of a country's exchange resources is not an essential element of a definition. For example, a government may restrict capital inflow by exchange control even though inflow would increase the country's monetary reserves. Similarly, the title of the legislation under which exchange control is imposed is not decisive. When a problem arises, a government may meet it with any statutory authority that is on the books under which exchange control can be justified, even though the statute does not specifically refer to exchange control. It has been seen already that the Fund's view of exchange control is a pragmatic one. Courts should accept the view of the Fund on what constitutes exchange control as the central authority in the field of exchange control under international law.

According to Chief Justice Fuller, speaking on behalf of the full United States Supreme Court:

Every sovereign State is bound to respect the independence of every other sovereign State, and the courts of one country will not sit in judgment on the acts of the government of another done within its own territory. Redress of grievances by reason of such acts must be obtained through the means open to be availed of by sovereign powers as between themselves.¹⁹

In formulating the Act of State doctrine, the Supreme Court of the United States in *Banco Nacional de Cuba v. Sabbatino*²⁰ declared that

rather than laying down or reaffirming an inflexible and all-encompassing rule in this case, we decide only that the Judicial Branch will not examine the validity of a taking of property within its own territory by a foreign sovereign government, extant and recognized by this country at the time of suit, in the absence of a treaty or other unambiguous agreement regarding controlling legal principles, even if the complaint alleges that the taking violates customary international law.²¹

The Hickenlooper Amendment to the Foreign Assistance Act of 1961, adopted as a reaction to the *Sabbatino* decision, declares that no

19. *Underhill v. Hernandez*, 168 U.S. 250, 252 (1897).

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

21. *Id.* at 428.

court in the United States shall refuse, on the ground of the federal Act of State doctrine, to make a determination on the merits giving effect of principles of international law in a case in which "a claim of title or other right to property" is asserted by any party, including a foreign state, "based upon (or traced through) a confiscation or other taking" by an act of that state in violation of the principles of international law.²²

The Hickenlooper Amendment applies to claims to "property" that has been confiscated contrary to international law, apparently when the property comes in to the territory of the United States.²³ The Amendment covers only a limited class of the range of cases in which the Act of State doctrine could apply.

In recent years, the courts have emphasized that the Act of State doctrine is derived not so much from the comity of nations as from the constitutional principle of the separation of powers. From this principle, it is deduced that the Judiciary must refrain from the embarrassment that it might create for the Executive in the conduct of foreign affairs. This rationale is said to explain the saving clause that refers to "a treaty or other unambiguous agreement regarding controlling legal principles" in the *Sabbatino* decision. If there is such a treaty or agreement, there is said to be no danger that the Judiciary will misconstrue the foreign policy of the Executive Branch.

The determination of the Supreme Court in the *Sabbatino* case to avoid an "inflexible and all-encompassing" definition of the Act of State doctrine has left room for suggested qualifications of the doctrine, although an exception to the doctrine based on a treaty or other unambiguous agreement seems to be more firmly rooted in the *Sabbatino* decision than most of the other alleged qualifications. It has been decided or asserted, for example, that the doctrine should not be applied if the State Department supports adjudication; and that the doctrine does not apply to the commercial activities of a foreign sovereign, to ministerial in contrast to governmental actions, to cases in which unjust enrichment would be the result of the doctrine, to acts of a state against its own citizens, or to cases in which a balancing of all factors deemed relevant, including the interests of the United States, leads to the conclusion that the doctrine should not be applied. The authors and commentators continue to debate whether these or other suggested exceptions are established law.²⁴

Attempts to make categorical assertions about the applicability of the act of state doctrine are bound to fail because the policies underlying the doctrine—preserving international comity and

22. The Foreign Assistance Act of 1961, 22 U.S.C. § 2370(e)(2) (1976).

23. Cooper, *Act of State*, *supra* note 18, at 293.

24. *See supra* note 18.

preventing embarrassment to the executive branch—can only be assessed by reference to the particular facts of a given case.²⁵

II. SOME U.S. CASES INVOLVING THE DOCTRINE AND EXCHANGE CONTROL

Theye y Ajuria v. Pan American Life Insurance Co.

The interrelationships of the exclusive currency of payment, exchange control, the Act of State doctrine, and the Fund's Articles, or the interrelationships of some of these elements, have been involved in a number of cases in the United States, including *Theye y Ajuria v. Pan American Life Insurance Co.*,²⁶ one of the so-called Cuban insurance cases.²⁷ In 1928, the plaintiff, who was a national and resident of Cuba, applied to the defendant, through its representative in Havana, for an insurance policy. The application was approved by the defendant's head office in New Orleans and the policy was delivered in Havana. The policy stipulated that the plaintiff would pay premiums, and the beneficiary would receive the proceeds of the policy, at the defendant's head office. In 1948, the Cuban Government adopted a law under which the Cuban peso was made legal tender for the discharge of all obligations, and, by decree adopted under the law, the U.S. dollar would cease to be legal tender in Cuba after 1951. The same decree provided that all contracts payable to or by Cuban nationals were to be paid, at par, in Cuban pesos only. The 1948 law made the peso legal tender; the subsequent decree made the peso the exclusive currency of payment.

In 1959, the Castro Government took office and introduced comprehensive exchange and other controls. In the same year, the defendant's assets in Cuba were nationalized. In 1960, after these legal measures, the plaintiff left Cuba as a refugee and demanded the cash surrender value of the policy at the defendant's head office, but the defendant refused to pay.

The defendant relied on various defenses, including the Act of State doctrine and the Fund's Articles. The trial court gave judgment for the plaintiff on the ground that the contract was subject solely to the law of Louisiana from the date the policy became a paid-up policy of insurance. The Court of Appeals of Louisiana (Fourth Circuit) reversed the judgment, citing it as a well established principle of law that a recognized foreign sovereign can make laws binding upon its nationals within its boundaries, a principle that sounds like the Act of State doctrine. The

25. Zimmerman, *Amorphous Doctrine*, *supra* note 18, at 560.

26. 245 La. 755, 161 So. 2d 70, *cert. denied*, 377 U.S. 997 (1964).

27. On the Cuban insurance cases, see 2 J. GOLD, *supra* note 2, at 43-94.

court supplemented this principle with two further considerations. First, the plaintiff had left Cuba after the 1959 exchange controls had been instituted, and, second, the Cuban Government had nationalized the defendant's assets in Cuba and had assumed all liabilities of the defendant. If the plaintiff were allowed to recover, the defendant would be required, in effect, to pay twice, because the Cuban Government had substituted itself as obligor and had taken over the defendant's Cuban assets to discharge the contractual liability to the plaintiff.

The court asserted, furthermore, that a sovereign has the power to change the situs of its nationals' contracts and to impair the obligations of those contracts. The court seems to have held that it had to apply all the propositions that it had cited because of Article VIII, Section 2(b), and that the court had to prevent the plaintiff from frustrating the will of the sovereign to which he owed allegiance. This solution had to prevail even if, before the Articles had come into existence, the plaintiff might have succeeded because the courts would not have given effect to exchange control regulations that were penal, punitive, confiscatory, or in violation of fundamental principles of justice.

The court's opinion was a mixture of the Act of State doctrine and the Fund's Articles, on the mistaken assumption that Article VIII, Section 2(b) requires courts to apply the doctrine. The court's reasoning seems to have been that the plaintiffs had been subject to the "police powers" of the Cuban Government when he left Cuba, and that Article VIII, Section 2(b) compelled the court to refuse the enforcement of a contract that was contrary to exchange control regulations imposed under those powers. The opinion rested on the exchange control regulations of 1959, and not on the laws that were in effect in 1928 and 1948.

Article VIII, Section 2(b) creates a defense that is distinct from the defense of the Act of State doctrine. The conditions for the application of the two defenses are not the same. Courts in the United States are working out the conditions for the application of the Act of State doctrine without reference to Article VIII, Section 2(b). The rationale based on the constitutional separation of powers is evidence that the Act of State doctrine owes nothing to Article VIII, Section 2(b) in the field of exchange control. If there is a point of contact between the two defenses, it is that Article VIII, Section 2(b) probably implies that the exchange control regulations of a member will not be recognized for the purpose of the provision by the courts of another member if the legislating member did not have jurisdiction to impose the exchange control regulations according to the standards of customary international law.²⁸

28. 2 J. GOLD, *supra* note 2, at 376-93.

The Supreme Court of Louisiana reversed the decision of the Court of Appeal in *Theye y Ajuria* and reinstated the decision of the trial judge. The law of Louisiana governed the contract, and Cuban laws adopted after the date the policy became a paid-up policy had no effect on the defendant's obligation as it existed on that date. The Supreme Court, citing another decision,²⁹ gave various reasons why Article VIII, Section 2(b) did not apply: the obligation antedated the Cuban exchange controls, the plaintiff had ceased to be a resident of Cuba, a contract for payment in U.S. dollars in Louisiana was not a foreign exchange contract, and the Articles did not displace the principle that the law of the place of performance chosen by the parties governs performance.

Of these arguments, the only one that carries weight is the change in the plaintiff's residence, as a result of which the balance of payments of Cuba was no longer affected by the contract. The Court of Appeal of Louisiana had placed major reliance on the Act of State doctrine. The Supreme Court of Louisiana gave the doctrine no weight, perhaps because the plaintiff, who had ceased to be a resident of Cuba, was entitled to payment in Louisiana, and, therefore, could not be affected by exchange control laws for which the doctrine was the alleged legal basis. To apply the doctrine to the plaintiff in these circumstances would be to apply it beyond what is deemed to be the reach of the legislating sovereign for the purpose of the doctrine.

The defendant's assets were nationalized, but the plaintiff was not deprived of all rights because payment in pesos at par was substituted for payment in U.S. dollars. What use the plaintiff could have made of the pesos did not arise. The question of the effect under the Articles of a limitation on transfer of the proceeds of the policy had they been paid in Cuba and the question whether the plaintiff's rights had been confiscated were not reached because of the court's interpretation of Article VIII, Section 2(b).

French v. Banco Nacional de Cuba

In *French v. Banco Nacional de Cuba*,³⁰ the New York Court of Appeals held that the imposition of exchange control by Cuba was within the Act of State doctrine in circumstances in which the plaintiff and her assignor, Ritter, were nonresidents of Cuba, but the place of performance, in contrast to the *Theye y Ajuria* case, was held to be within Cuba. Ritter, an American citizen, was resident in Cuba when he invested U.S.

29. *Blanco v. Pan American Life Insurance Co.*, 221 F. Supp. 219 (S.D. Fla. 1963), *modified*, 362 F.2d 167 (5th Cir. 1967). See also *Pan American Life Insurance Co. v. Blanco*, 311 F.2d 424 (5th Cir. 1962); 2 J. GOLD, *supra* note 2, at 48-53.

30. 23 N.Y.2d 46, 242 N.E.2d 704, 295 N.Y.S.2d 433 (1968).

dollars in the purchase of a farm in Cuba. At that time, the Cuban Government permitted foreign investors to disinvest and obtain U.S. dollars or other foreign currency, which could be transferred abroad free of the tax applied on the export of currency. The Currency Stabilization Fund of the Cuban Government was authorized to issue "certificates of tax exemption" to investors. Ritter obtained eight certificates. Each of them recited that Ritter or his endorsee would receive from the Banco Nacional de Cuba, against delivery of a stated amount of pesos and on surrender of the certificate, "a check on New York for an equal amount of United States Dollars," exempt from the exportation tax. The certificates were signed by both the defendant (the Banco Nacional) and the Stabilization Fund.

On July 15, 1959, the Stabilization Fund suspended "for the time being" the processing of the certificates. Ritter applied for payment in U.S. dollars but payment was refused. The holders of certificates could receive pesos. The plaintiff had received the certificates by assignment from Ritter. She obtained judgment on them in the Supreme Court of New York, and judgment was affirmed by the Appellate Division. The defenses of sovereign immunity and the Act of State doctrine were rejected by the Appellate Division.

The Court of Appeals was unanimous in deciding that the defense of sovereign immunity could not be sustained, because the activities from which the action arose were commercial in character. Four of the seven members of the court held that the refusal to provide U.S. dollars for pesos was a breach of contract and an Act of State. Both the Banco Nacional and the Currency Stabilization Fund were treated as agencies of the Cuban Government.

Chief Judge Fuld, with whom three other judges concurred, then turned to the question of whether the Hickenlooper Amendment precluded application of the Act of State doctrine. The Court held that an exchange control regulation that altered the value or character of the money to be paid in satisfaction of contractual obligations was not a "confiscation" or "taking" within the meaning of the Hickenlooper Amendment, because Ritter was not deprived of anything that qualified as "property." Ritter held pesos and a contract, which was to be performed in Cuba and was subject to Cuban laws. Ritter was not entitled to U.S. dollars or a specific fund of dollars held by another (a "traceable" fund). The Cuban Government had not assumed title to a contractual right or other chose in action belonging to Ritter.

Nothing in the lengthy record of the congressional proceedings suggests that the amendment was designed to cover claims of breach of contracts by a foreign government such as the one in

this case. Nor was there any intimation that Congress had in view the highly complex problems of exchange control regulations, repudiation of debts or depreciation of currency. Conspicuously absent from the hearings was the kind of expert testimony on international monetary problems which surely would have been sought if the Congress had been addressing itself to problems of that nature.³¹

Chief Judge Fuld recalled that the Senate Report on the Hickenlooper Amendment had explained the reference to "property" in the Amendment to demonstrate that the word did not apply to contractual claims. The report stated that the word was inserted

to make it clear that the law does not prevent banks, insurance companies and other financial institutions from using the act of state as a defense to multiple liability upon any contract, deposit or insurance policy in any case where such liability has been taken over or expropriated by a foreign state.³²

The Hickenlooper Amendment, the Chief Judge continued, did not displace the Act of State doctrine, and neither did the reservation for any "treaty or other unambiguous agreement regarding controlling legal principles" in the *Sabbatino* formulation. A footnote pointed out that the only treaty that might have been applicable was the Articles of Agreement of the Fund, but Cuba had withdrawn from membership in 1964.³³ This withdrawal made it possible for Chief Judge Fuld to concentrate on customary international law as it applied to the case before him:

In short, the control of national currency and of foreign exchange is an essential governmental function; the state which coins money has "power to prevent its outflow". . . and as the court observed in *Perry v. United States*, 294 U.S. 330, 356. . . , "[t]he same reasoning is applicable to the imposition of restraints upon transactions in foreign exchange. . . ." The Restatement finds no violation of international law in such a currency measure "if it is reasonably necessary in order to control the value of the currency or to protect the foreign exchange resources of the state. . . ." The Restatement goes on to recite that "the application to an alien of a requirement that foreign funds held within the territory of the state be surrendered against payment in local currency at the official rate of exchange is not wrongful under international law, even though the local currency is less valuable on the free market than the foreign funds surrendered." Thus, if the Cuban Government

31. 23 N.Y.2d at 60, 242 N.E.2d at 714, 295 N.Y.S.2d at 447.

32. 23 N.Y.2d at 61, 242 N.E.2d at 714, 295 N.Y.S.2d at 448.

33. 23 N.Y.2d at 55, n. 6, 242 N.E.2d at 710, n. 6, 295 N.Y.S.2d at 442, n. 6.

could, under the example cited, have properly required an alien within its borders to surrender American dollars "against payment" in pesos, as a measure "reasonably necessary. . .to protect the foreign exchange resources of the state". . .the present refusal of the Cuban Government to surrender American dollars in order to protect its dollar reserves, though harsh in effect, would also seem to be within the limits of international legality.³⁴

On the basis of this statement of customary international law, the Chief Judge concluded that, even if the case were understood to involve "a claim of title or other right to property" within the meaning of the Hickenlooper Amendment, the Act of State doctrine would not have been set aside, because Cuba had not violated international law.³⁵

If Cuba had remained a member of the Fund, it would have been necessary to see to what extent the somewhat tentative statement of customary law quoted above had been modified by the Articles of the Fund. The provisions of the Articles on restrictions, and perhaps on multiple currency practices and discriminatory currency arrangements, would have been pertinent.

Judge Keating, with whom two other judges concurred, dissented on the ground that the case involved not a breach of contract but a confiscation of property in the disguise of a valid exchange control regulation. The word "property" in the Hickenlooper Amendment covered the deprivation of contractual rights suffered by the plaintiff.

Weston Banking Corporation v. Turkiye Bankasi, A.S.

In *Weston Banking Corporation v. Turkiye Bankasi, A.S.*,³⁶ the defendant relied on both the Act of State doctrine and the Fund's Articles to resist the plaintiff's claim. The plaintiff, a Panamanian banking corporation, sought to enforce a promissory note signed, on July 9, 1976 in Istanbul, by representatives of the defendant, a Turkish bank. Neither party did business in New York. Under the terms of the note, the defendant undertook to repay the plaintiff an amount of Swiss francs on July 9, 1979 plus interest payable semiannually. Payments of principal and interest were to be made at the offices of the Chemical Bank in New York City by means of a cable transfer to Switzerland in Swiss currency.

34. 23 N.Y.2d at 63-64, 242 N.E.2d at 715-16, 295 N.Y.S. at 449-50.

35. Hopkins J., with whom three other judges concurred, expressed the opinion that the breach of contract by Cuban authorities was an Act of State and that there would have been no need for the authorities to cite the exchange control provisions as justification. Burke J., with whom two other judges concurred, dissented on the ground that the defendant had not proved that the exchange control provision that had been cited applied to the certificates in issue. 23 N.Y.2d at 64-76, 242 N.E.2d at 716-23, 295 N.Y.S.2d at 450-60.

36. 57 N.Y.2d 315, 442 N.E.2d 1195, 456 N.Y.S.2d 684 (1982).

The payments were to be "made clear of all restrictions of whatsoever nature imposed thereon by, outside of bilateral or multilateral payment agreements or clearing agreements which may exist at the time of payment and free and clear of and without deductions for any taxes, levies, imposts, deductions. . .imposed. . .by the Republic of Turkey."

Again under the terms of the note, the defendant designated the Chemical Bank in New York City as its legal domicile and accepted the jurisdiction of the New York courts, but agreed that the plaintiff would have an option to bring suit in the Turkish courts. The final paragraph of the note stated that it was issued under Communiqué No. 164 published by the Ministry of Finance of Turkey.

The communiqué amended Decree No. 17 of the Ministry. The effect was that a private bank in Turkey was allowed to open deposit accounts in convertible Turkish liras (CTLDs) when the bank obtained foreign currency by borrowing or through deposits. The foreign currency had to be transferred to the central bank, which credited the private bank with the equivalent in Turkish liras. The Turkish Government guaranteed the private bank against fluctuations in exchange rates, so that the private lender or depositor and the private bank would suffer no exchange loss on repayment of the loan or withdrawal of the deposit.

In July 1976, the defendant borrowed an amount of Swiss francs from the plaintiff and opened a CTLD. Interest was paid in accordance with the terms of the note, but in July 1979 the defendant refused to pay the principal because regulations enacted by Turkey after the date of the note permitted repayment only in liras and consequently barred repayment in Swiss francs.

The majority of the Court of Appeals of the State of New York gave judgment for the plaintiff. The majority distinguished *French v. Banco Nacional de Cuba* and followed *Zeevi & Sons v. Grindlays Bank Ltd.*³⁷, the next case discussed in this article, in holding that a debt is not located within a foreign state unless that state has the power to enforce or collect the debt. In the *Weston* case, the debt was equally capable of being enforced against the defendant's assets in New York and its assets in Turkey. The Act of State doctrine did not prevent recovery of a debt situated in New York.

The force of this conclusion is reduced somewhat by the court's finding that, on the documents submitted by the defendant, it had not been proved that the Turkish regulations relied on by the defendant did

37. 37 N.Y.2d 220, 371 N.Y.S.2d 892, 333 N.Y.2d 168, *cert. denied*, 423 U.S. 866 (1975). The court cited *Republic of Iraq v. First National City Bank*, 353 F.2d 47 (2d Cir. 1975) as further authority because the Federal court held that the Act of State doctrine is confined to governmental action affecting property within the government's territory.

prevent Turkish banks from paying with foreign currency the kind of note on which the plaintiff was suing. The regulations merely established a program for restructuring the debt through the central bank, to which program the plaintiff could have had recourse if it chose.

For this same reason, the plaintiff's claim was not unenforceable under Article VIII, Section 2(b). "[A] different case would have been presented" if it had been proved that the regulations prevented payment in foreign currencies on the liquidation of a CTLD.³⁸

Judge Meyer delivered a strong dissenting opinion in which he concluded, on his reading of all the Turkish regulations and his understanding of Article VIII, Section 2(b), that the provision did apply. The consequence, in his view, was that neither the Act of State doctrine nor the intention of the parties to insulate their contract from Turkish exchange control regulations was relevant.³⁹

Zeevi & Sons v. Grindlays Bank Ltd.

In the *Zeevi* case,⁴⁰ which was followed in the *Weston* case, an Israeli corporation, on March 24, 1972, deposited Ugandan currency with the defendant to establish a fund against which an Israeli firm, the plaintiff's assignor, could draw. On the same date, the defendant opened an irrevocable credit in an equivalent amount of U.S. dollars under which the plaintiff could draw in specified monthly installments. Payments were to be made to the plaintiff by the defendant's agent bank in New York City.

In March and April 1972, the central bank of Uganda, acting with the authority of the Minister of Finance under the exchange control legislation of Uganda, notified the defendant that foreign exchange allocations to Israeli companies and nationals were to be cancelled and that no foreign exchange payments were to be made to these entities. The defendant notified its agent bank and the plaintiff of this directive. The defendant refused to make payments requested by the plaintiff's New York bank. In an action by the plaintiff, the defenses included the Act of State doctrine and Article VIII, Section 2(b).

The court emphasized the importance to those engaged in commerce of having a reliable place of payment in a financial capital. It was equally important to protect the interests of New York City as a financial center, from which the court deduced that its law was to be paramount in deciding the legal issues in the case. The court held that the discrimina-

38. 57 N.Y.2d at 326, 442 N.E.2d at 1200, 456 N.Y.S.2d at 689.

39. 57 N.Y.2d at 328-29, 442 N.E.2d at 1201, 456 N.Y.S.2d at 690.

40. See *supra* note 37.

tory and confiscatory directive adopted after the issuance of the letter of credit was contrary to the public policy of the State of New York. Furthermore, the Act of State doctrine was inapplicable, because a debt is not located within a state unless that state has the power to enforce or collect it. The debt in this case was situated in New York City and was beyond the reach of Uganda. The court summarily rejected the defense based on the Articles on the ground that a letter of credit is not an "exchange contract." To hold that an exchange of Ugandan currency for U.S. dollars was not an "exchange contract" would seem not to narrow that expression but to deprive it of all content.

The facts in the case do not demonstrate any disposition by the Ugandan authorities merely to interrupt for the time being performance of the obligation to complete the exchange. On the contrary, the facts suggest that the authorities intended to prevent performance of the defendant's obligation at any time. The central bank's message to the defendant on March 28, 1972 was that payments to Israeli entities "should not be processed until clearance had been obtained from the undersigned." On April 13, 1972, the defendant was informed that "[t]here can never be any basis for the expenditure of foreign exchange unless value in the form of goods has been received in Uganda." The directive had nothing to do with legal tender or exchange control. The directive applied to Israeli payees only and it was not confined to payments within Uganda. Nothing in the reported facts demonstrated that the plaintiff or its assignor could import goods into Uganda.

Allied Bank International v. Banco Credito Agricola de Cartago

*Allied Bank International v. Banco Credito Agricola de Cartago*⁴¹ was an action against three Costa Rican banks, which were wholly owned by the Government of Costa Rica. The plaintiffs were Allied Bank, a bank chartered in the United States with its principal place of business in New York City, and a syndicate of 39 banks, which had designated Allied Bank to pursue the action on their behalf. The three defendants had executed a series of promissory notes payable to the syndicate banks. Payments were due every six months through July 1983 and were to be made in New York City. Failure to pay an installment of interest or principal within 30 days after the specified date would constitute default, and the plaintiff could then demand payment in full. If failure to pay resulted from the omission or refusal of the central bank

41. 566 F. Supp. 1440 (S.D.N.Y. 1983), *aff'd*, 733 F.2d 23 (2d Cir. 1984). (EDITOR'S NOTE: The opinion of the United States Court of Appeals, Second Circuit, published in the advance sheet at 733 F.2d 23-27, was withdrawn from the bound volume because rehearing was granted.)

to release U.S. dollars, default would be excused for a further 10 days. The defendants agreed to be sued in New York or in Costa Rica. All payments were made before July 1981, but then, in response to an economic crisis, the Costa Rican Government imposed exchange controls under which the approval of the central bank was required for any foreign exchange transactions on the part of the banks.

On July 2, 1981, one of the defendants applied to the central bank for authorization to enter into a foreign exchange transaction that would enable the applicant to make the payment that had become due on July 1, 1981. Before the defendant had received a reply, the central bank passed a resolution on August 27, 1981 prohibiting public sector entities, such as the defendants, from paying interest or repaying principal denominated in foreign currency on debts to foreign creditors.⁴² On November 6, 1981 the President of Costa Rica and the Ministry of Finance published a decree preventing any institution in Costa Rica from making payment on an external debt without prior approval of the central bank acting in consultation with the Ministry of Finance. The decree stated that the Government was engaged in "renegotiating its External Debt and for this purpose there should be harmony of decisions and centralization in the decision-making process." On November 9, 1981, the central bank refused the authorization requested on July 2, 1981, and later informed all three defendants that they would not be allowed to make repayments of external debt until Costa Rica's difficulties with external debt were resolved.

The defendants advanced a number of defenses, including sovereign immunity and the Act of State doctrine. The United States District Court for the Southern District of New York held that the defense of sovereign immunity failed because the defendants' execution of the promissory notes was a commercial activity. The court held, however, that the defense of Act of State must succeed because payment was prevented by the directives of the central bank, the President, and the Ministry of Finance. Their actions were public in character, and not commercial. The court held that the actions "were undertaken in response to a serious national economic crisis, and . . . were of the type which some governments undertake to try to assist in such a crisis—*i.e.*, restrictions upon foreign currency transactions."⁴³ If the court were to reject the doctrine, the court would risk embarrassing relations between the Executive Branch of the United States and the Government of Costa

42. Except for payments to multilateral international agencies and then only to the extent that resources in foreign exchange were available.

43. 566 F. Supp. at 1443.

Rica. The place of payment in this case, as in the *Weston* case, was New York City, but Judge Griesa in the *Allied* case reached a different result.

The decision of the lower court was affirmed by the United States Court of Appeals for the Second Circuit on April 23, 1984, but on the basis of a different rationale.⁴⁴ The appellate court noted that while the action was still pending in the district court, negotiations had begun for the rescheduling of payments under the defendants' obligations. On September 9, 1983, after dismissal of the action by the district court, the plaintiffs, the Government of Costa Rica, and the central bank had signed a refinancing agreement with the coordinating agent for Costa Rica's external creditors. Only one of the 39 banks in the syndicate, Fidelity Union Trust Company of New Jersey, refused to join in the agreement. It was only this bank that Allied Bank represented as an agent on appeal. The defendants were honoring the refinancing agreement and had made payments to the other 38 banks in accordance with it.

The court stated that Costa Rica's economic crisis had caused the default not only on the payments to the plaintiffs but also on payments under the country's intergovernmental obligations.⁴⁵ When a country defaults on a loan by the United States under the Foreign Assistance Act of 1961,⁴⁶ further aid to that country by the United States is barred unless the President advises Congress that assistance is in the national interest.⁴⁷ The President had advised that

[c]ontinuation of U.S. assistance to Costa Rica is consistent with the commitment of this Administration and in Congress to help Costa Rica regain economic viability. We therefore regard such assistance, which is designed to help the Government with financial and management reforms and with needed credit to the private sector, as vital and in the national interest. We are hopeful that bilateral debt restructuring will be completed within the next several months.⁴⁸

The House of Representatives also expressed its full support for Costa Rica and its democratic institutions as that country responded to its economic crisis. In January 1983, the United States joined other nations in signing a Paris Club Agreed Minute⁴⁹ to reschedule the intergov-

44. *Allied Bank Int'l v. Banco Credito de Cartago*, 733 F.2d 23 (2d Cir. 1984) [hereinafter cited as *Allied Bank*]. See note 41 *supra*.

45. *Id.* at 25.

46. Act for International Development of 1961, Pub. L. No. 87-195, 75 Stat. 424.

47. 22 U.S.C. § 2370(q) (1982).

48. *Allied Bank*, *supra* note 44, at 25.

49. INTERNATIONAL MONETARY FUND, IMF STAFF TEAM, RECENT MULTILATERAL DEBT RESTRUCTURINGS WITH OFFICIAL AND BANK CREDITORS, Occasional Paper 25 (1983). See also INTERNATIONAL MONETARY FUND, EXTERNAL INDEBTEDNESS OF DEVELOPING COUNTRIES, Occasional Paper 3 (1981).

ernmental debt of Costa Rica. The Agreed Minute contained a provision recommending the rescheduling of Costa Rica's commercial obligations.

The plaintiffs argued that the Act of State doctrine, which the district court had applied, was not applicable because the situs of the debts was New York City. The Court of Appeals found it unnecessary to consider this contention.

When the property or contractual obligations affected by the foreign government's actions are located within the United States, our courts will give effect to those actions "only if they are consistent with the policy and the law of the United States."⁵⁰

Therefore, even if the situs of the debts was in the United States, the actions of the Costa Rican Government will be recognized if they are consistent with the law and policy of the United States. The actions of the Costa Rican Government that resulted in the prohibition of payments on external debt met this test. The court based its application of public policy on the situs of the debts in the United States⁵¹ and apparently not on any principle that the law of New York governed the contracts under private international law.

The court cited a decision of the Supreme Court of the United States holding that New York bondholders were bound by the Canadian Government's reorganization of the debts of the Canada Southern Railway, which was government-owned.⁵² The Supreme Court held in that case that the plan was in harmony with the spirit of bankruptcy laws, which were recognized by all civilized countries, including the United States. International comity required recognition of foreign plans of the kind involved in the Canadian reorganization.⁵³

The Court of Appeals in *Allied Bank* referred to Chapter 11 of the U.S. Bankruptcy Code⁵⁴ as a further analogy.

Costa Rica's prohibition of payment of debt was not a repudiation of the debt but rather was merely a deferral of payments while it attempted in good faith to renegotiate its obligations.⁵⁵

On the basis of these analogies and the finding that Costa Rica's actions were consistent with the law and policy of the United States, the court held that the validity of Costa Rica's actions should be recognized by

50. *Allied Bank*, *supra* note 44, at 26.

51. *Id.*

52. *Canada Southern Railway Co. v. Gebhard*, 109 U.S. 527 (1883).

53. *Id.* at 539.

54. 11 U.S.C. §§ 1101-74 (1982). See also Oechsli, *Procedural Guidelines for Renegotiating LDC Debt: An Analogy to Chapter 11 of the U.S. Bankruptcy Reform Act*, 21 VA. J. INT'L L. 305 (1981).

55. *Allied Bank*, *supra* note 44, at 26.

courts in the United States.⁵⁶

Finally, the court rejected the argument that Costa Rica's actions should not be recognized because the Government was acting as a commercial entity and not as a sovereign.⁵⁷ The court held that although the actions affected commercial activity, Costa Rica was clearly acting as a sovereign in preventing a national financial disaster.⁵⁸

Early newspaper reports mentioned the surprise and apprehension that the decision provoked. There were rumors that a request for a rehearing had been made.⁵⁹ The President of the Federal Reserve Bank of New York is reported to have said that "Fed lawyers expect. . . [the] decision to be overturned. The ruling effectively allows troubled, debtor countries to unilaterally stop paying their debts, leaving lending banks without legal recourse."⁶⁰

The United States as *amicus curiae* submitted a brief in support of a petition for rehearing and suggestion for rehearing en banc, in which the United States asserts that the decision is based on a misunderstanding of the policy of the United States.⁶¹ The brief alleges that the President's certification dealt with the continuation of U.S. assistance notwithstanding default on loans by the United States to the Government of Costa Rica and did not deal with private commercial debt. The Paris Club Agreed Minute was a multilateral understanding among creditor nations recommending common terms for the bilateral restructuring of Costa Rica's debts to participating governments. The Minute contained only a recommendation to the Costa Rican Government to seek the restructuring of debt to private creditors on comparable terms. The concurrent resolution of the House of Representatives was a general statement of sympathy for the Costa Rican Government in responding to its economic crisis.

None of these actions, the brief declares, suggests that Costa Rican debt to private creditors should be rendered unenforceable by actions of the Costa Rican Government to which creditors did not agree. The policy of the United States places great weight on the voluntary participation of private lenders in the process of restructuring debt. This process is an element in the orderly resolution of the problems of debt service

56. *Id.* at 27.

57. *Id.*

58. *Id.*

59. Gilpin, *Ruling on Costa Rica Raises Debt Questions*, N.Y. Times, Apr. 27, 1984, at D1, col. 1. See also Witcher, *Appeals Court Rule May Allow Nations to Renege on Some Debts to U.S. Banks*, Wall St. J., Apr. 27, 1984, at 2, col. 3; Hall, *U.S. Ruling on Costa Rica Worries Bankers*, Financial Times (London), Apr. 30, 1984, at 1.

60. Wall St. J., May 4, 1984, at 6, col. 3.

61. Brief of the United States, as *amicus curiae*, at —, *Allied Bank Int'l v. Banco Credito de Cartago*, 733 F.2d 23 (2d Cir. 1984). See note 41 *supra*.

faced by many developing countries. An orderly resolution is crucial to the stability and future growth of the economy of the world and of the United States.

The brief sets forth, as follows, the five points of the strategy that the United States Government has been following in response to the problem of debt service:

- (1) economic adjustment by borrowing countries designed to stabilize their economies and restore sustainable external positions; (2) an International Monetary Fund (IMF) adequately equipped to help borrowers design adjustment programs and provide balance of payments financing on a temporary basis while adjustment programs take effect; (3) readiness of monetary authorities in creditor countries to provide short-term liquidity support, when essential to assist selected borrowers that are formulating adjustment programs with the IMF; (4) encouragement to private markets to provide prudent levels of financing to borrowing countries in the process of implementing IMF-supported adjustment programs; and (5) resumption of sustainable, non-inflationary economic expansion and maintenance of open markets, both in the industrial countries and in developing countries facing debt problems.⁶²

The United States Government expressed its concern that the process it was supporting would be jeopardized by the court's decision. An important element in the functioning of the process was the willingness of commercial banks to reschedule debt and to provide credit to countries undertaking adjustment efforts. The confidence of lenders in the enforceability of agreements payable in New York was critical to their willingness to extend commercial debt. The uncertainties created by the decision might discourage commercial lenders from providing essential new financing and could deter the pursuit of adjustment.

The decision has created dismay because it appears to give a foreign country a unilateral right to impose a deferment of indebtedness, both public and private, that will be recognized by U.S. courts as consistent with U.S. public policy. The decision endorses another kind of unilateralism that has not been criticized. The Court of Appeals referred to the law and policy of only the United States. The court regarded the restructuring of debt as analogous to bankruptcy and reorganization, but the plaintiff was unable to recover because Costa Rica's exchange control prevented payments except in accordance with the restructuring. An international test of public policy, consistency with the Fund's Articles in relation to the exchange control of Costa Rica as a member of the Fund,

62. *Id.* at — . See note 41 *supra*.

was available and could have been recognized.⁶³ This was a test of public policy that should have been recognized. The force of the test does not depend on whatever may be the fate of the *ratio decidendi* in the *Allied* case.

The court made no reference to the Articles or to membership of the United States and Costa Rica in the Fund. Had the court applied the international public policy that can be drawn from membership in the Fund and the consistency of exchange control regulations with the Articles, and not merely the national public policy of the United States, the case would have been an addition to the jurisprudence that includes *Perutz v. Bohemian Discount Bank in Liquidation*,⁶⁴ *Kolvrat v. Oregon*,⁶⁵ and *Banco Frances e Brasileiro S.A. v. Doe*.⁶⁶ The New York Court of Appeals in *Perutz* and *Banco Frances* and the Supreme Court of the United States in *Kolvrat* drew normative principles from the Articles because of the membership in the Fund of the United States and of another country whose exchange control regulations were involved in the proceedings and were consistent with the Articles. In no one of the three cases was the holding based on Article VIII, Section 2(b).

In 1965, I wrote of two of the three cases and a third that is not cited here that:

They show that it is not only the express provisions of the Articles that can have an impact on private parties. The transactions of such parties can be quite seriously affected by principles of public policy that are deduced from the general effect of the Articles. The consequences can be felt on contracts even though the case is not one that would fall within the scope of Article VIII, Section 2(b). Moreover, the effects may penetrate into areas of private international law in which contracts are in no way involved.⁶⁷

Some years later, I wrote that:

Courts in adopting restrictive interpretations of Article VIII, Section 2(b) and in neglecting public policy as an independent basis for relief are not merely failing to give effect to the consequences of interdependence but are acting in opposition to the

63. The brief of the U.S. Government as *amicus curiae* mentions the Fund's efforts to promote adjustment, but draws no inference from this function in relation to exchange control. *Id.* at —. See note 41 *supra*.

64. 304 N.Y. 533, 110 N.E.2d 6 (1953), discussed in 1 J. GOLD, THE FUND AGREEMENT IN THE COURTS 28-30, 50-55 (1962) [hereinafter cited as 1 J. GOLD].

65. 366 U.S. 187 (1961); discussed in 1 J. GOLD, *supra* note 64, at 128-35.

66. 36 N.Y.2d 592, 331 N.E.2d 502, 370 N.Y.S.2d 534 (1975); discussed in 2 J. GOLD, *supra* note 2, at 197-202.

67. J. GOLD, THE INTERNATIONAL MONETARY FUND AND PRIVATE BUSINESS TRANSACTIONS: SOME LEGAL EFFECTS OF THE ARTICLES OF AGREEMENT 31 (IMF Pamphlet Series No. 3, 1965); See also 2 J. GOLD, *supra* note 2, at 106, 155, 221-30.

actions of their governments. . .What is now proposed is that courts should weigh the interests of other members of the Fund when issues related to international monetary relations arise in litigation. There are circumstances in which the public policy of the *lex fori* should dictate concern for the interests of other contracting parties even though there is no specific provision of the Articles that compels this concern.⁶⁸

These recollections do not imply that the loan contract in the *Allied* case was not an "exchange contract" or that Article VIII, Section 2(b) was inapplicable. The views are recalled to restate the proposition that there is an international public policy in relation to exchange control even when the provision does not apply. Furthermore, international public policy should be recognized by members as national public policy by virtue of their membership in the Fund.

Membership and the consistency of exchange control regulations with the Articles as the touchstone for public policy would avoid the absurdity of assuming that the approach taken by the Court of Appeals was confined to the circumstances of the case. The court referred to an intergovernmental default under the Foreign Assistance Act of 1961 and the response of the President in his advice to Congress. There might be no intergovernmental default in circumstances in which nevertheless the imposition of exchange control affected payments under loan agreements. The international and national interest in the economic recovery of the country imposing the exchange control might be just as strong in these circumstances as in cases involving intergovernmental default. There would be no logic in requiring intergovernmental default as a condition of recognizing the force of public policy. It is less obvious, however, that widespread agreement on the restructuring of debt should not be a condition for the recognition of the public policy that is advocated here. What is meant by "widespread" is itself a problem.

The *Allied* court dwelt on the need, as a matter of public policy, to respect the exchange control regulations of a country that had received financial assistance from the United States and might receive further assistance. It was pointed out some years ago that it was odd for courts in the United States to adopt restrictive interpretations of Article VIII, Section 2(b) or of public policy that prevented the recognition of the exchange control regulations of a country that was receiving financial assistance from the Fund with resources subscribed by the United States.⁶⁹ Financial assistance and temporary exchange restrictions were

68. 2 J. GOLD, *supra* note 2, at 221-22.

69. See 1 J. GOLD, *supra* note 64, at 139; 2 J. GOLD, *supra* note 2, at 28, 30.

part of a comprehensive program to enable a member to overcome its balance of payments difficulty.

The decision implies the rejection of a defense based on classification of exchange control laws as "revenue" laws. This classification has induced courts to react negatively to the exchange control laws of other countries.⁷⁰ The New York Court of Appeals has referred to the principle on which this reaction is based as an "old chestnut," and though the court was unable because of precedent to hold that nothing remained of the principle, the court was able to impose a radical limitation on its scope.⁷¹ The New York court stated that:

Nothing in the agreement [the Articles] prevents an IMF member from aiding, directly or indirectly, a fellow member in making its exchange regulations effective. And United States membership in the IMF makes it impossible to conclude that the currency control laws of other member States are offensive to this State's public policy so as to preclude suit in tort by a private party [because of alleged conspiracy to evade Brazil's exchange control regulations]. Indeed, conduct reasonably necessary to protect the foreign exchange resources of a country does not offend against international law. . . Moreover, where a true governmental interest of a friendly nation is involved—and foreign currency reserves are of vital importance to a country plagued by balance of payments difficulties—the national policy of co-operation with Bretton Woods signatories is furthered by providing a State forum for suit.⁷²

The decision of the Court of Appeals of the Second Circuit in the *Allied* case can imply one of three reactions to exchange control laws and "revenue" laws. First, exchange control laws are not properly classifiable as revenue laws. Second, refusal to recognize revenue laws applies only to the enforcement of them and not to the recognition of them for other purposes. Recognition for the purpose of refusing to decree the performance of contracts that are contrary to exchange control laws does not amount to the enforcement of the regulations. Third, the "old chestnut" has now disappeared.

Other questions are raised by the decision, but, though noted, they are not pursued here. Would the principle enunciated by the court apply if the country imposing exchange control is not a member of the Fund? The Articles confine the benefit of Article VIII, Section 2(b) to members. Moreover, Article XI, Section 2 distinguishes between members and non-

70. See *Banco do Brasil, S.A. v. A.C. Israel Commodity Co., Inc.*, 12 N.Y.2d 371, 190 N.E.2d 235, 239 N.Y.S.2d 872 (1963); 2 J. GOLD, *supra* note 2, at 24-25.

71. 36 N.Y.2d at 596, 331 N.E.2d at 505, 370 N.Y.S.2d at 537-38.

72. 36 N.Y.2d at 598, 331 N.E.2d at 506, 370 N.Y.S.2d at 539.

members by enabling members to impose restrictions on exchange transactions with nonmembers, or with persons in the territories of nonmembers, unless the Fund finds that restrictions prejudice the interests of members and are contrary to the purposes of the Fund.

Another question that arises is whether the signing of a Paris Club Agreed Minute that recommends the rescheduling of a debtor country's commercial obligations falls under the second sentence of Article VIII, Section 2(b):

In addition, members may, by mutual accord, cooperate in measures for the purpose of making the exchange control regulations of either member more effective, provided that such measures and regulations are consistent with the Agreement.⁷³

Once again, this question would arise only if contracts did not fall under the first sentence of Article VIII, Section 2(b).

Yet another question that deserves consideration arises because the defendants in the cases were wholly owned by the Government of Costa Rica. If the defendants were considered part of the apparatus of government, according to whatever criteria were appropriate for reaching that conclusion, would the exchange controls constitute "restrictions" on payments and transfers for current international transactions for which the approval of the Fund was necessary? The Fund's practice distinguishes between restrictions, on the one hand, and defaults by governments on their own obligations that the Fund has no authority to approve, on the other hand.⁷⁴

Libra Bank Limited v. Banco de Costa Rica

*Libra Bank Limited v. Banco de Costa Rica*⁷⁵ is another case decided by the United States District Court for the Southern District of New York that involved an international loan transaction and the exchange control regulations of Costa Rica. In this case, however, the court dealt not only with the Act of State doctrine but also with the Articles of the Fund. On the Act of State doctrine, the court reached a result that was consistent with the *Weston* case and inconsistent with the decision of Judge Griesa in the *Allied* case.

The Libra Bank, which was organized under the laws of the United Kingdom and had a representative office in New York City, acted as agent for 16 banks in making a loan of \$40 million to the defendant, a bank wholly owned by the Government of Costa Rica. Libra Bank

73. Articles of Agreement, *supra* note 1.

74. INTERNATIONAL MONETARY FUND, 1983 ANNUAL REPORT ON EXCHANGE ARRANGEMENTS AND EXCHANGE RESTRICTIONS 37 (1983).

75. 570 F. Supp. 870 (S.D.N.Y. 1983).

brought this action on behalf of seven other plaintiffs. Six of these plaintiffs were organized under the laws of countries other than the United States, each in a different country. Of the six, two had offices in New York City. The seventh plaintiff was a national banking corporation of the United States. The seven lenders brought this action to recover their shares of the principal amount of the loan, plus interest. The plaintiffs sought an order for summary judgment, relying on the promissory notes issued in connection with the loan.

The purpose of the loan was to provide pre-export and export financing for Costa Rican sugar and sugar products. The loan was to be repaid in New York City in four successive monthly installments during 1981. The defendant consented to the jurisdiction of the New York courts and to construction of the terms of the agreement in accordance with New York law. The payments were to be made free and clear of, and exempt from, charges and withholdings with respect to performance.

The proceeds of the loan were paid to the defendant's account at a bank in New York City. The defendant made the first scheduled repayment on July 30, 1981 and paid interest until August 1981, but made no further repayments of principal or payments of interest after that date.

The defendant declared that it had been denied authorization to make payments in foreign currency under the exchange control law of Costa Rica (which has been referred to above in the discussion of the *Allied* case). The defendant asserted that the court was barred from entering judgment by the Act of State doctrine. The plaintiffs replied that the doctrine applies only when a foreign sovereign appropriates property within its own territory, but the situs of the property in question was in the United States. Further, if *prima facie* the doctrine did apply, the case was within the exception relating to commercial activity.

The court decided that the plaintiffs' right to repayment of the debt was situated in New York City. Costa Rica was not able to exercise exclusive dominion over the plaintiffs' right, because the New York courts could enforce or collect it against the defendant's assets in New York City. The court rejected the defendant's argument that the decrees did not confiscate property but merely prevented the defendant from repaying the debt. The court's refusal to distinguish between tangible assets and intangible assets in the form of contractual rights and the court's treatment of contractual rights as "property" for the purpose of the Act of State doctrine are in conflict with the majority opinion in the *French* case. Moreover, the court assumed that there was a confiscation even though the Costa Rican Government did not purport to take over the plaintiffs' right. Perhaps the court considered that the benefit the govern-

ment obtained by withholding the foreign exchange necessary for payment was equivalent to confiscation.

It is not clear whether the assumption of confiscation rested on the hypothesis that the Government of Costa Rica was repudiating indebtedness—which might have been Uganda's intention in the *Zeevi* case—and was not simply delaying payment until the exchange crisis was over. Governments do not intend, when they impose exchange control, to divest parties of their contractual rights. Contracting parties may be offered payment in the national currency instead of the contractual currency of payment, or payment may be postponed for the time being. In the less likely event that the national currency has been interposed as the exclusive, that is to say compulsory, currency of payment, there may be a stronger case for concluding that there has been a divestiture of rights. Before this conclusion is reached, the rights attached to the exclusive currency in the hands of the payee should be examined. The self-interest of governments precludes divestiture because this action would undermine and perhaps ruin their creditworthiness. The court offered no analysis of the character of Costa Rica's exchange control.

In this case, no inquiry appears to have been made into the possibility that Costa Rica intended to negotiate a restructuring. Nor was any attention paid to the Fund's approval of a stand-by arrangement for Costa Rica on December 21, 1982. An objective of a stand-by arrangement in such circumstances is the elimination of arrears and the resumption of the servicing of external debt,⁷⁶ in accordance with any restructuring if it has been established by agreement with creditors. The Fund's press release announcing its approval of the stand-by arrangement contained the following sentence:

The 1983 economic adjustment program, which the stand-by arrangement supports, is designed to contain inflationary pressures, to promote an orderly development of the exchange mar-

76. SELECTED DECISIONS, *supra* note 7, at 243-45. The Fund's policy on payments arrears, reproduced in these pages, contains the following, para. 4 at 245:

Fund financial assistance to members having payments arrears should be granted on the basis of performance criteria or policies with respect to the treatment of arrears similar to the criteria or policies described in the preceding paragraph for the approval of the payments restrictions. In general, the understandings should provide for the elimination of the payments arrears within the period of the stand-by arrangement. Such understandings should be based on the concept of a given level of payments arrears and should be reflected in the performance criteria included in stand-by arrangements in the higher credit tranches. To support the policies designed to deal with arrears the letter of intent should include a statement that there would be no imposition of new restrictions or increase in the level of delayed payments. Where Fund financial assistance is being provided, but only through the first credit tranche, the adoption of a viable program directed toward the elimination of the payments arrears should be an important factor in considering whether the country was making reasonable efforts to redress its international financial situation.

ket, and to allow for the resumption of foreign debt service payments.⁷⁷

The court, having concluded in the *Libra* case that the Act of State doctrine was not relevant, held that there was no need to consider the argument that commercial activity was an exception to the doctrine and that this exception was applicable in the circumstances of the case.

The court moved on to questions of the interpretation of the contract, which need not be discussed here. Finally, the court considered a defense based on Article VIII, Section 2(b), which the defendant introduced on July 15, 1983, the day on which the court had been prepared to enter summary judgment for the plaintiff. The court decided that a contract to borrow dollars and repay in the same currency in New York City was not an "exchange contract" within the meaning of the provision. The court also questioned whether the contract, if considered an exchange contract, can become unenforceable as the result of exchange control regulations imposed after the contract had been entered into. Lastly, the court held that the defendant had not discharged the burden of proving that the exchange control regulations were maintained or imposed consistently with the Articles, which made all the other reactions to Article VIII, Section 2(b) *obiter dicta*.

It remains to be seen what effect the decision of the Court of Appeals in the *Allied* case, or any further decision in that proceeding, will have on the *ratio decidendi* of the *Libra* case.

III. SOME INTERRELATIONS AMONG ACT OF STATE, PUBLIC POLICY, AND THE FUND'S ARTICLES

The confiscation of property is not a precise concept, but, however it is defined, it is likely that all governmental acts covered by an accepted definition would be deemed to fall within the Act of State doctrine as applied in the United States, if the conditions of that doctrine were satisfied. If confiscation is defined as the divestiture of property, including

77. INTERNATIONAL MONETARY FUND, Press Release No. 82/70 (1982). In the *Weston* case, no inquiry was made into Turkey's relations with the Fund, although stand-by arrangements were approved on April 24, 1978, July 19, 1979, and June 27, 1983. The Prime Minister of Turkey made the following statement in an interview published in January 1984:

Let me tell you this: Our own recovery program and the IMF suggestions actually parallel each other. Both are addressing the century-old Turkish problem of the foreign exchange bottleneck and balance of payments. Without balance-of-payments improvement, we cannot improve the GNP. And as for unemployment, we know that with a real rate of growth of around 7 percent this unemployment will decrease—not by much, but gradually. In any case, to achieve a strong balance-of-payments situation, there was and will be no other alternative but to follow the IMF program. It has helped Turkey start to pay its debt and interest payments. And it has allowed us to borrow intelligently from the market. Marton, *The Rough Road Ahead for Turgut Ozal*, INST'L INVESTOR Jan. 1984, at 106 (int'l ed.).

contractual rights, confiscation should not be considered exchange control under the Articles. Exchange control may change or postpone performance of a party's rights, but he is not divested of those rights.

The Act of State doctrine applies to a foreign government's action only if the contacts deemed relevant by the forum for the application of the doctrine are connected with the government's territory. Courts may not agree on the contacts they deem relevant. Whatever the contacts may be, they may differ from those that determine whether the exercise of exchange control is legitimate. For example, other governments may consider it admissible for the government of Patria to regulate by exchange control the payments that its residents are allowed to make with assets outside the territory of Patria, but this governmental action might not be considered an Act of State. Exchange control is intended normally to conserve foreign exchange resources. U.S. dollar balances, for example, are held in the United States. It would be meaningless to recognize the concept of exchange control and decide that exchange control could not affect resources that are held by the legislator's residents outside the territory of the legislator.

The defense on which a defendant is likely to rely when he invokes the Articles is that discharge of his obligation is impeded by exchange control regulations and that his contract is unenforceable as the result of Article VIII, Section 2(b). That provision contains a number of conditions that must be met if reliance on it is to succeed: the contract must be an "exchange contract," the contract must be contrary to "exchange control regulations," the contract must "involve" the currency of the member that has "maintained or imposed" the exchange control regulations, and the regulations must be consistent with the Articles. The maintenance or imposition of exchange control regulations, though not confiscation, is governmental action that could be considered an Act of State if the conditions of the doctrine were met, but the conditions of Article VIII, Section 2(b) need not be satisfied. For example, the doctrine may apply to the exchange control of contracts that are not "exchange contracts," particularly if a narrow interpretation of that concept prevails.

The cases discussed above show that defendants in the United States have tended to place primary reliance on the Act of State doctrine, although the *Allied* case may give an impetus to the defense of public policy if the decision in that case is not reversed. Sometimes, the possible relevance of Article VIII, Section 2(b) does not occur to the defendant or occurs to him late in his response to the plaintiff's claim.

The scope of the Act of State doctrine and the exceptions to it are still the subject of differences among courts and among legal scholars.

The interpretation of Article VIII, Section 2(b) also is subject to much controversy, because to date the Fund's only interpretation of the provision deals with no more than a few aspects of it.⁷⁸ Courts in the United States have tended to restrict the scope of Article VIII, Section 2(b) and to ignore the international interests that the provision is meant to serve. The interpretation of the provision requires some understanding of the objectives of the Articles and of the economic difficulties and setbacks that may occur in pursuing the objectives. Article VIII, Section 2(b) is included in a multilateral treaty, and therefore the decisions of foreign courts and the writings of foreign legal scholars, properly evaluated, should be considered an aid to the understanding of the provision. It is not surprising that the legal advisers of defendants are more confident in advancing the Act of State doctrine, notwithstanding the uncertainties surrounding it, than they are in dealing with Article VIII, Section 2(b).

Can some order be suggested in the confusing interrelationships among the exclusive currency of payment, exchange control, the Act of State doctrine, public policy, and the provisions of the Fund's Articles? An attempt is made in the following paragraphs:

1. Governmental obstruction of the discharge of a contractual obligation in accordance with its terms is not necessarily exchange control. A distinction should be observed between the transformation of an obligation or the postponement of its discharge and the divestiture of rights. Divestiture should not be considered exchange control within the meaning of the Articles. Article VIII, Section 2(b) does not apply to divestiture, but the Act of State doctrine would apply if the conditions for its application were met. The *Zeevi* case may be an illustration of the first part of this proposition, although the court did not make this point.

2. A member's prescription of its currency as the exclusive currency for making payments must be examined in the context of a member's restrictive and exchange system to see how the Articles treat the prescription. The prescription is not necessarily *cours légal* or *cours forcé* legislation only, because the prescription may also be a restriction under the Articles.

3. The Articles are a treaty binding on the United States, which has given the force of law to Article VIII, Section 2(b). For this reason, the courts should consider the effect of such a provision before examining a defense based on the judicial doctrine of the Act of State.⁷⁹ Further-

78. SELECTED DECISIONS, *supra* note 7, at 233-34.

79. For earlier discussions of the relationship between the Articles and the Act of State doctrine, see Paradise, *Cuban Refugee Insureds and the Articles of Agreement of the International Monetary Fund*, 18 U. FLA. L. REV. 74-77 (1965), and Williams, *Extraterritorial Enforcement of Exchange Control Regulations under the International Monetary Fund Agreement*, 15 VA. J. INT'L L. 387-94 (1975).

more, the court should take judicial notice of the effect of the provision even when not raised as a defense.⁸⁰ There is no need to invoke public policy to justify the duty of the court to raise the issue. In the *Weston* case, Judge Meyer insisted on the court's duty to raise the issue of Article VIII, Section 2(b), because the provision expressly requires the United States as a member of the Fund to treat certain contracts as unenforceable. If the court finds that the contract is unenforceable as a result of the provision, the plaintiff must fail.

4. It has been seen that there are numerous conditions that must be met in order to demonstrate that Article VIII, Section 2(b) is applicable. The restrictive interpretations of these conditions favored by some courts are unfortunate because they frustrate the objectives of the provision. Suppose, however, that the court finds, for whatever reason, that Article VIII, Section 2(b) does not apply. A court should turn next to the question of public policy as recognized in the *Allied* case or, preferably, as based on some broader principle. The justification for treating public policy as next in the order of defenses is clear if public policy is based on a broader principle derived from the Articles as a treaty binding on the United States. If, however, public policy is applied according to a purely national criterion, the *Allied* case shows that the defense of public policy demands examination before the Act of State doctrine is considered because public policy applies whether or not application of the doctrine can be sustained.

5. If a court holds that neither Article VIII, Section 2(b) nor public policy is a valid defense, the defense of Act of State should be considered next in the hierarchy of defenses. It might be argued, however, that Article VIII, Section 2(b) has replaced the Act of State doctrine in the field of exchange control. This conclusion has been reached by an English appellate judge in discussing the principle that English courts will not enforce claims under contracts made in England and on their face lawful under English law if they require the performance of acts in another country that are unlawful there. Lord Justice Stephenson said:

[T]he Bretton Woods Agreement lays down the standard—or requirements—of comity in the area of exchange control which it covers: whether it extends to states who are not members of the International Monetary Fund or parties to the Agreement we do not have to consider. Article VIII, Section 2(b) displaces the common law principle, as was clearly the opinion of Diplock L.J. in *Sharif v. Azad*, . . . with which I respectfully

80. *United City Merchants (Investments) Ltd. v. Royal Bank of Canada*, [1982] 2 W.L.R. 1050; 2 J. GOLD, *supra* note 2, at 114-15, 118-19.

agree.⁸¹

If this view implies that contracts are enforceable notwithstanding the exchange control regulations of another member whenever Article VIII, Section 2(b) does not apply, it would have to be objected that the provision prescribes unenforceability only and not enforceability. In any event, Lord Justice Stephenson's view is unlikely to be favored in the United States because his view is based solely on comity, while the Act of State doctrine in the United States rests on the constitutional separation of powers as well as comity.

6. If a court is considering the defense of an Act of State, the *Sabotino* doctrine may come into play. To apply that doctrine, the court would have to find that "a taking of property" is involved. If that expression is confined to the actions that have been called divestiture, the expression does not cover exchange control. Divestiture may seem to be the normal understanding of "a taking of property."

It is possible, however, that a more extensive meaning might be given to the expression. Perhaps a court might hold that exchange control in the form of Patria's substitution of its own currency as the exclusive currency of payment or the postponement of payment in the contractual currency is a detriment to the plaintiff and a benefit to Patria that could be considered a "taking."⁸²

The attitude to Costa Rica's exchange control in the *Libra* case and the minority view of Judge Keating in the *French* case would have to be accepted to support the conclusion that there is a "taking." Furthermore, if the contractual place of payment is outside the legislator's territory, it would be necessary to follow the lead of Judge Griesa in the *Allied* case in holding that the Act of State doctrine can apply even to such a case. These requirements may be formidable barriers for a defendant to surmount when relying on the doctrine.

If, nevertheless, the court decides that the case involves a "taking" and that the Act of State doctrine applies, the court must then decide whether there exists "a treaty or other unambiguous agreement regarding controlling legal principles." The cases do not support the theory that the Supreme Court, by means of this phrase, was reserving for future decision the question whether there is an exception or qualification to the Act of State doctrine when such a treaty or agreement is applicable. The Supreme Court is understood to have been expressing a normative princi-

81. *United City Merchants (Investments) Ltd v. Royal Bank of Canada*, [1981] 2 W.L.R. 259; 2 J. GOLD, *supra* note 2, at 344-45; *see also Id.* at 200, 352-53.

82. *See* Christie, *What Constitutes a Taking of Property under International Law*, 28 BRIT. Y.B. INT'L L. 307 (1962); Sohn & Baxter, *Responsibility of States for Injuries to the Economic Interests of Aliens*, 55 AM. J. INT'L L. 553 (1961).

ple and not the reservation of an unsettled point of law for further inquiry.

The Fund's Articles are a treaty that might be understood to establish "controlling legal principles." Two questions arise: first, what do the "controlling legal principles" control, and, second, is the treaty "unambiguous?" The answer to the first question appears to be that the controlling legal principles control the international validity of the "taking." Validity is no longer determined by customary international law but now depends on consistency with the Fund's Articles as the applicable treaty. The Articles are not ambiguous in determining when exchange control measures are consistent with the Articles. The measures are consistent when approved by the Fund or authorized by the Articles. An interpretation of the Articles is not necessary to establish consistency, but an inquiry addressed to the Fund is necessary to discover whether or not the Fund has approved an exchange control measure or has not granted approval because the measure is authorized by the Articles. In short, it is necessary to discover how the Fund has exercised its regulatory authority. The court should not substitute itself as the international regulatory authority by treating the question of consistency with the Articles as one of interpreting the Articles. The members of the Fund, including the United States, have agreed by treaty that the Fund exercises the discretionary authority conferred on it.

The line of thought pursued here might result in a decision that, because a "taking" was consistent with the Articles, the plaintiff could not recover, even though the result was not required by Article VIII, Section 2(b). The plaintiff's inability to recover might seem anomalous in such circumstances. The consequences of the "taking" would be dictated by U.S. law as expressed in the *Sabbatino* case, however, and not by the Articles.

A court, after arriving at the conclusion that an exchange control regulation was a "taking" and that the Articles provide the controlling legal principles, might be tempted to take an alternative route, so as to avoid the apparent anomaly mentioned in the preceding paragraph. The court might hold that the question of validity for the purpose of the *Sabbatino* principle was not concluded by a finding that the exchange control measure was consistent with the Articles because it was approved by the Fund or authorized by the Articles. The controlling legal principle would be Article VIII, Section 2(b). This approach would avoid one anomaly by relying on another. The hypothesis on which the court was considering the Act of State doctrine, according to the proposed hierarchy of defenses, would be that Article VIII, Section 2(b) had been found inapplicable in the first instance. Now, the same inquiry would be made

for the purpose of the Act of State doctrine and would lead to the same result.

The alternative theory discussed in the preceding paragraph is undermined by a further flaw. The controlling legal principle in the *Sabbatino* formulation relates to validity under the applicable treaty or agreement, but although Article VIII, Section 2(b) requires consistency with the Articles as a condition for application of the provision, Article VIII, Section 2(b) does not determine consistency.⁸³

7. The alternatives discussed in 6 above subject the expression "a taking of property" to some strain in extending it to exchange control. It would be preferable to recognize a parallel formulation for applying the Act of State doctrine to exchange control. The phrase "exchange control" would be substituted for "a taking of property" in the *Sabbatino* formulation. A problem that would arise at once would be the meaning of "within its own territory." Two meanings are possible in relation to contracts: the exchange control regulation applies to the contracts of residents within the territory of the legislator of the exchange control or the regulation applies to payments that contracting parties are required by their contracts to make in that territory.

The first meaning would be broader than the second and would be preferable because its breadth would give greater scope to the international public policy as expressed by the Articles. The second and nar-

83. The second alternative would raise another issue. The Supreme Court's reference to "a treaty or other unambiguous agreement" is itself ambiguous. The problem is not whether the adjective "unambiguous" is attached to "agreement" only and not to "treaty." The normal meaning of the phrase is that both the treaty and the agreement must be unambiguous. The problem is whether the court was referring to the existence of an applicable treaty or to the clarity of the provisions of an obviously applicable treaty. There can be no doubt that the Articles deal with the international validity of exchange control regulations. If Article VIII, Section 2(b) were deemed to be the provision that establishes the controlling legal principle, a court should not forgo the judicial function of interpreting a relevant provision to see how it applies in the circumstances of the case before the court. (The caveat must be repeated, however, that the question of the consistency of exchange control regulations with the Articles is one that depends on administration by the Fund and not on interpretation of the Articles.) The argument against the exercise of the judicial function is the possible embarrassment of the U.S. Administration in its conduct of foreign relations because the other country might not concur in the court's interpretation. The other country and the United States, however, are members of the Fund, and experience shows that members accept the fact that courts are called on to interpret the provisions of the Articles.

The United States District Court for the Western District of Michigan reached a different conclusion in *Ethiopian Spice Extraction Company v. Kalamazoo Spice Extraction Company*, 543 F. Supp. 1224, 1230 (W.D. Mich. 1982) on the judicial function:

The terms used in § 2 are so inherently general, doubtful, and susceptible of multiple interpretation that in the absence of an established body of law to clarify their meaning a court cannot reasonably be asked to apply them to a particular set of facts.

The United States Court of Appeals for the Sixth Circuit reversed the lower court's decision on March 9, 1984, but on the ground that the treaty provision in question was not ambiguous. *Kalamazoo Spice Extraction Company v. Provisional Military Government of Socialist Ethiopia*, 729 F.2d 422 (6th Cir. 1984).

rower meaning would be more compatible with the traditional view of the territorial contact necessary for the application of the doctrine.

For the reasons discussed above, the "treaty or other unambiguous agreement regarding controlling legal principles" should be understood in relation to exchange control to be the provisions of the Articles that determine the consistency of exchange control regulations with the Articles. These provisions do not include Article VIII, Section 2(b).

8. The relationship of exchange control and "taking" can arise in circumstances in which the Act of State doctrine is not applicable. The problem of this relationship is most obvious when a member applies controls to balances of the member's currency held by nonresidents at the time when the controls are imposed or that are received by nonresidents later. It has been noted above that the divestiture of property rights, including contractual rights, should not be considered exchange control. The implications of this view are that the Articles do not give a member the privilege of divesting nonresidents of their balances of currency, even if the Articles permit a member to postpone use of the balances or even to change the rights attached to them. The provisions of the Articles suggest that a member may prohibit the transfer of the proceeds of current international transactions with the temporary approval of the Fund but must permit transfer after the approval comes to an end. If a member imposes controls on capital balances, it should not be held that the Articles authorize the member to deprive the holders of all use of the balances. Whether sufficient use is permitted to prevent the member's action from being considered a taking should be decided on the basis of the facts.

9. The approach in the discussion of the hierarchy of defenses is influenced to a substantial extent by the conviction that the disregard of internationally approved or authorized exchange control is a form of isolationism that neglects the interests of the world economy. Exchange control can impose hardship on private activities and is rebarbative for that reason. Nevertheless, the members of the Fund have agreed that international interests can be served by exchange control as a temporary measure when approved or authorized in accordance with the Articles. There is a fundamental inconsistency between the governmental recognition of these interests and the judicial disregard of them.