February 1966

International Law--Present Status of the Act of State Doctrine and Its Effects upon Private Foreign Investment

Larry Lynn Skeen
West Virginia University College of Law

Follow this and additional works at: https://researchrepository.wvu.edu/wvlr

Part of the International Law Commons

Recommended Citation
Available at: https://researchrepository.wvu.edu/wvlr/vol68/iss2/24

This Student Note is brought to you for free and open access by the WVU College of Law at The Research Repository @ WVU. It has been accepted for inclusion in West Virginia Law Review by an authorized editor of The Research Repository @ WVU. For more information, please contact ian.harmon@mail.wvu.edu.
International Law—Present Status of the Act of State Doctrine and Its Effects upon Private Foreign Investment

Every sovereign state is bound to respect the independence of every other sovereign State, and the courts of one country will not sit in judgement 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.¹

This statement in Underhill v. Hernandez has come to be recognized as the classic pronouncement of the Act of State doctrine. In essence the United States Supreme Court held that a victim of expropriation by a foreign power could recover only through action by the Executive branch. Thus State Department negotiations and


[ 168 ]
settlement rather than court action was held the proper course for recovery of the value of property seized without compensation by a foreign state.\textsuperscript{2} Act of State was first invoked by name in the Underhill case in 1897. Underhill, an American whose Venezuelan waterworks had been seized by a revolutionary general, instituted a suit for damages in a United States court. On appeal the Supreme Court held each nation sacrosanct regarding decrees affecting property within its borders. Consequently, Underhill's only recourse for compensation was State Department championing of his cause.\textsuperscript{3} The Act of State doctrine was hinted at in earlier decisions, but Underhill has become known as the genesis of the doctrine.\textsuperscript{4} Since Underhill, Act of State has been applied in a variety of situations.\textsuperscript{5}

Only one notable exception to the use of Act of State has occurred.\textsuperscript{6} In the Bernstein decisions the State Department influenced the second circuit to decide the case on its merits rather than apply the Act of State doctrine where a German Jew's property was expropriated by a war-time Nazi nationalization decree. The Bernstein exception has not found further extension and application in other situations, probably as a result of the extenuating character of wartime Nazi policies toward its Jewish nationals.\textsuperscript{7} Act of State does not extend to recognition of the penal and fiscal laws and decrees of other states. Practices regarding the effect and necessity of in personam judgments also vary.\textsuperscript{8} The doctrine has been applied even where the forum state finds the uncompensated seizure violated its concepts of international justice.\textsuperscript{9}

\textsuperscript{2} Ibid.
\textsuperscript{3} Ibid.
\textsuperscript{6} Bernstein v. Van Heyghen Freres, S.A., 163 F.2d 246 (2d Cir. 1947), cert. denied, 332 U.S. 772 (1947); accord, Bernstein v. Nederlandsche-Americaansche Stoomvart-Maatschappij, 210 F.2d 375 (2d Cir. 1954), amending per curiam, 173 F.2d 71 (2d Cir. 1949).
\textsuperscript{7} Dep't State Press Release No. 298, April 27, 1949; 20 Dep't State Bull. 592 (1949).
\textsuperscript{9} Cases cited note 5, supra.
In the nineteenth and early twentieth centuries, decisions involving expropriations were occasional if not infrequent. When they did occur, they usually involved the seizure of vessels. Presently the complex interactions between the world powers, plus the emergence of many new states which formerly were protectorates and colonies, have created more numerous controversies involving nationalization and expropriation. The newly emergent nation-states have been striving to improve their resources and assets by self-help, sometimes necessitating confiscations in their view. The socialist states follow a policy of nationalization with subsequent state control of industry. The fear of loss generated by such seizures has thwarted many would-be private foreign investors although the larger American concerns and those willing to risk a loss of investment have found the profit from their foreign endeavors to be substantially worth the risk.

Where an industry or enterprise is nationalized without discrimination as to ownership, compensation sometimes has been meted out to the United States Government for the benefit of the confiscation victims. Where, however, American investments are expropriated or seized as a method of reprisal, little voluntary remuneration, if any, is generally forthcoming.

One of the main justifications of Act of State is that foreign settlements of United States claims is the responsibility of the Executive department. To allow recovery in the courts, it is reasoned, could lead to the embarrassment of the Executive branch and result in incongruous policies toward foreign neighbors. This postulate has created the quandry facing the courts in foreign confiscation controversies because in the fulfillment of its responsibility the State Department has met with less than credible success. Invariably, by United States standards, the compensation for the seized property is neither prompt nor adequate.

In a trail of recent litigation the Act of State doctrine has been raised for judicial examination and reconsideration. To better understand the present status of United States law regarding foreign confiscations, an examination of this litigation is necessary.

10 Paul, supra note 4, at 699-701, 707-09.
11 Ibid.
13 65 Colum. L. Rev. 531, 532 (1965).
14 Wright, supra note 12, at 314.
The Sabbatino Trail

As a reprisal against United States reduction of sugar imports from Cuba, Castro's government in 1960 nationalized the Cuban located property of twenty-six American concerns. Among the twenty-six was the sugar producer Compania Azucarera Vertientes-Camaguey de Cuba (CAV)-a Cuban incorporated concern in which United States investors owned more than ninety per cent of the outstanding stock. At that time a shipment of CAV sugar was being loaded for shipment to Farr, Whitlock and Company, a United States concern with which CAV had executed a contract of sale. Not until Farr-Whitlock had renegotiated the same agreements with the Cuban government was the ship permitted to depart for Casablanca. Cuban representatives then sent the bills of lading to New York for negotiation. Farr-Whitlock gained control of the bills of lading, negotiated them and paid the proceeds to Peter Sabbatino, a New York receiver appointed for CAV. Then Banco Nacional de Cuba brought a federal suit in the southern district of New York against Farr-Whitlock for conversion of Cuban property, and against Sabbatino for an injunction to freeze the assets until that court could decide the outcome.\textsuperscript{15} The suit by Banco Nacional de Cuba was the reverse of the normal situation where the plaintiff is an American seeking redress for property seized by a foreign state. Here, the seizing state was seeking recognition of its act of seizure. The district court held the Act of State doctrine inapplicable where a violation of international law had been committed. The bases of the decision were that the seizure was unrelated to a public purpose, discriminatory and without adequate compensation. The second circuit affirmed, adding that messages from the State Department to counsel made application of the Act of State doctrine unnecessary.\textsuperscript{16}

The Supreme Court reversed and remanded the case, anticipating that the funds held by Sabbatino would be paid to the alien property custodian who held all Cuban assets in the United States.\textsuperscript{17} The Court therefore held in favor of the Banco Nacional de Cuba as the governmental representative of Cuba. The Court stated that although not required by the Constitution or by principles of international law, the Act of State doctrine was a part of federal com-

\textsuperscript{16} Banco Nacional de Cuba v. Sabbatino, 307 F.2d 845 (2d Cir. 1962).
\textsuperscript{17} Banco Nacional de Cuba v. Sabbatino, 376 U.S. 395, 428 (1964).
mon law binding on both state and federal courts. Reasons advanced by the Court gave great deference to the fact that the political branch of the United States Government was responsible for United States foreign policy. The Court believed that an adverse judicial determination based upon recognized principles of international law could hinder any attempted recovery by the State Department as well as embarrass it in the conduct of foreign affairs. This decision was reached despite the apparent illegality of the uncompensated seizure and regardless of the tenor of relations between the two states involved. Some writers labelled the Sabbatino decision an act of abstention by the Court, but technically the plaintiff won the decision. Continued recognition of Act of State in the United States would have been assured if the lower Court had been able to carry out the instructions of the Supreme Court. However, the judiciary was not left alone to effect an outcome.

THE SABBATINO AMENDMENT

Before the case was decided upon remand, Congress acted swiftly and silently. Although a number of jurists reacted favorably to the decision, many scholars questioned the wisdom of the Supreme Court decision. Reacting to the latter criticism and in order to bolster government foreign investment guaranties to Americans contained in the Foreign Assistance Act of 1964, Congress in effect reversed the Sabbatino decision in part by a rider to the Foreign Assistance Act. Congress provided that American courts should not apply Act of State and that they should apply instead principles of international law regarding any case occurring after January 1, 1959, unless: (1) the foreign act was not contrary to international law; (2) the claimant's right was based upon an irrevocable letter of credit issued not more than 180 days before the confiscation; or (3) the Executive branch specifically invoked the Act of State doctrine by filing with the court a suggestion to that effect. To further clarify its intent, Congress informed the courts by the legislation

18 Ibid.
19 Ibid.; Paul, supra note 4, at 694-95.
20 Paul, supra note 4, at 695.
21 65 COLUM. L. REV. 530 (1965).
22 Ibid.
24 Paul, supra note 4, at 691.
that its view of international law included prompt, adequate and
effective compensation.25

No hearings were held on this amendment by the Senate Foreign
Relations Committee, and no criticism was made on either the House
or Senate floor. A roll call vote was never requested.26 The amend-
ment was sponsored by Senator Hickenlooper, who made the only
audible airings about the bill.27 The effect of the rider is to reverse
the Sabbatino holding (therefore requiring application of interna-
tional law by United States courts) except where the President
informs the court that foreign policy interests can best be served by
applying the Act of State doctrine in a particular case.28

One main purpose of the amendment is to allow federal and state
courts freedom in applying international law, including the concept
of prompt and adequate compensation for expropriated property.29
Protecting American investment abroad, checking the flow of confis-
cated property into the United States and discouraging foreign con-
fiscations are other purposes.30 The rider consequently provides the
private litigant a forum for suing or defending against a confiscating
foreign state or its representative.31 Many authorities harbor grave
doubts whether the amendment will in fact protect foreign invest-

25 Foreign Assistance Act § 301(d)(4), 78 Stat. 1013, 22 U.S.C. § 2370-
1965 U.S. CODE CONG. & AD. NEWS 3263, 3267: "(2) Notwithstanding any
other provision of law, no court in the United States shall decline on the ground
of the federal act of state doctrine to make a determination on the merits giving
effect to the 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 (or a
party claiming through such state) based upon (or traced through) a confisca-
tion or other taking after January 1, 1959, by an act of that state in violation of
the principles of international law, including the principles of compensation and
the other standards set out in this subsection: Provided, That this subparagraph
shall not be applicable (1) in any case in which an act of a foreign state is not
contrary to international law or with respect to a claim of title or other right to
property acquired pursuant to an irrevocable letter of credit of not more than
180 days duration issued in good faith prior to the time of the confiscation or
other taking, or (2) in any case with respect to which the President determines
that application of the act of state doctrine is required in that particular case
by the foreign policy interest of the United States and a suggestion to this effect
is filed on his behalf in that case with the court."
remarks of Senator Hickenlooper); Friedmann, Sabbatino in the Courts and
in Congress, 3 COLUMN J. TRANSNAT'L L. 103 (1965).
29 Id. at 532.
30 Ibid.; Henkin, Sabbatino in the Courts and in Congress, 3 COLUMN J.
TRANSNAT'L L. 107, 113 (1965); 65 COLUMN L. REV. 530, 532-33 (1965).
31 Statute cited note 25, supra.
ment and strengthen the influence of international law.\textsuperscript{32} The favorite tools of diplomats—negotiation and compromise—better lend themselves to favorable settlement than does litigation in many cases. This situation is true because of the rare circumstances where the parties, property and other requirements of jurisdiction can be satisfied in domestic courts.

The amendment is not limited to Americans whose property has been seized abroad.\textsuperscript{33} Any individual may avail himself of federal and state courts as a result of the language used in the amendment.\textsuperscript{34} This opening of the court doors to foreign as well as domestic victims could flood the courtrooms if too many foreign claims were pressed in reliance upon the amendment. Use of United States courts by foreign litigants also could harm the United States image in the nation of the litigant's allegiance, and if some of the expropriated property were still in possession of the confiscating government or governments an unfavorable court decision could hinder State Department compensation negotiations already in progress.\textsuperscript{35}

\textbf{Policy Considerations}

American courts always have maintained some mistaken impressions regarding the necessity of compensation where property is nationalized or expropriated.\textsuperscript{36} This proposition is still far from settled. The Supreme Court in \textit{Sabbatino} held that no universal agreement supports the principle that compensation must follow expropriation of foreign located property. The notion of compensation is more prevalent in western nations than eastern, and it is advanced more by the "have" nations rather than the "have nots."\textsuperscript{37} Despite this ambivalence, the requirement of compensation appears in the Hickenlooper amendment.\textsuperscript{38}

The new power vested in the President to interfere and to require the application of Act of State also should be studied. Requiring the application of the doctrine in one circumstance and refraining from

\textsuperscript{32} 65 \textit{COLUM. L. REV.} 530, 532 (1965); Henkin, supra note 30, at 107, 110.
\textsuperscript{33} Henkin, supra note 30, at 113.
\textsuperscript{34} 65 Statute cited note 25, supra.
\textsuperscript{35} 65 \textit{COLUM. L. REV.} 530, 532-33 (1965).
\textsuperscript{37} Paul, supra note 4, at 705-08.
\textsuperscript{38} Statute cited note 25, supra.
its use in another might elicit cries of favoritism or discrimination from foreign neighbors. This interference also could weaken the influence of American court decisions on international law, notwithstanding the question of separation of powers that the rider provokes.

Another question raised by Sabbatino and the subsequent amendment is whether domestic courts rather than international tribunals should entertain international disputes concerning expropriations. Sabbatino indicates that both state and federal courts properly can entertain jurisdiction. The amendment affirms this view.

The increasing need of stable, predictable international principles for use by all nations has been advanced in support of the Sabbatino decision. Advocates of this view maintain their position although Act of State is invoked where an expropriation is admittedly in violation of the forum nation's concepts of international justice. The fluctuating foreign policy of the United States has been detrimental to the United States foreign image for years, and Sabbatino supporters believe the preferable approach to be a non-vacillating policy by the judiciary regarding treatment of foreign confiscatory decrees.

Political emotions at the time of the Sabbatino controversy cannot be ignored. United States relations with the Cuban government were at a low ebb. When foreign relations are beset by conflict there is a natural tendency in the courts of any nation to decide in favor of their own nationals. The United States Supreme Court resisted this temptation. The desirability of maintaining a constant image toward other states often necessitates decisions not in harmony with public opinion. In a stable world composed of highly civilized, legally sophisticated nations of corresponding ideologies, Act of State would be an excellent legal principle. That the world has not yet reached such a Utopia is apparent. Nevertheless, progress toward international legal stability cannot be made unless some participants are willing to risk present self-denial and indignation for possible future good. The Sabbatino decision may have been dec-

40 Henkin, supra note 30, at 114.
41 Banco Nacional de Cuba v. Sabbatino, 376 U.S. at 428; Paul, supra note 4, at 694; 65 COLUM. L. REV. 530, 537 (1965).
42 Henkin, supra note 30, at 115.
43 Ibid.
44 Friedmann, supra note 28, at 103-104.
ades ahead of its time rather than a detriment to international law as its critics contemplate. However, as varying degrees of civilization still exist, the question still persists: would it not be better for the advanced nations to decide expropriation cases on their merits when dealing with an underdeveloped nation?

Some authorities consider that policy or goal-value oriented interpretations of international law which postulate that all participants in the world arena seek to maximize their own values are not in accord with the Sabbatino decision. The inclination of this school is the temporary adoption of a rule or policy best suited to benefit the forum court's participants at the time of the controversy. This view is predicated upon the belief that the more judicially sophisticated nations should decide international disputes in compliance with their own concepts of justice rather than allow a judicially unsophisticated nation to effect a different outcome. At times such a view leads toward identification of international law with national interests. Because the Cuban expropriation was a discriminatory reprisal in the eyes of Americans, the goal oriented decision would favor those participants blessed with a more advanced concept of human dignity—the American stockholders. The domestic benefits to be derived from the policy oriented decision are evident, but the international repercussions of such a result also should be considered, especially by a nation seeking to spread its concepts of justice and fair play.

Heterogeneous philosophies and ideologies are more prevalent in society today, thus resulting in a variousness of jurisprudential systems. This variousness is necessarily a factor in any judicial determination of international law. These conflicts of ideology render any controversy a delicate diplomatic tightrope. The larger powers must accept the fact that newer, previously unfamiliar concepts of legitimacy attend the basic governmental structure of many newly emergent sovereignties. Increased governmental participation in international affairs by many of these states, as well as their increasing engagement in foreign business transactions, indicates a possible trend. In many eastern European and Asian governments, state trading already has become the custom. Trans-

---

national bartering by governments (rather than by individuals) evidences the need for settled standards of treatment regarding the sale by these governments of previously expropriated goods. Where the nationalization of property by a state tends to relieve the tax burdens of its citizenry, the doctrines of sovereign immunity and Act of State seem more applicable. The Tate Letter of 1952, pertaining to United States future foreign policy, declared the State Department would not recommend immunity for a foreign state trading confiscated goods when the transaction was essentially a commercial one. The difficult definition of what constitutes a commercial transaction is left to judicial and State Department interpretation.

Opponents of the Act of State doctrine insist a decision in domestic courts should be made on the merits of a claim where the seizure is believed against principles of international law. They contend that the resultant decisions could not be as embarrassing to United States foreign policy as imagined. Such a decision, they suggest, could be used as a bargaining factor to American advantage where the State Department is attempting settlements. State Department efforts usually have not resulted in complete success. Nevertheless, they have resulted in occasional substantial compensations to expropriation victims. State Department efforts, therefore, cannot be overlooked, especially in a world where not all nations recognize a duty to promptly and adequately compensate victims of confiscation.

Had it not been for the enactment of the Hickenlooper amendment, the federal court on remand would have applied the Act of State doctrine in favor of plaintiffs as directed by the Supreme Court. However, the amendment was found to apply to litigation remanded to the United States District Court for Southern New York. The district court held that the Hickenlooper amendment did not violate the fifth amendment even when applied to a case remanded by the Supreme Court. The court held that the amend-

48 Id. at 100-01; 4 VA. J. INT'L L. 75 (1964).
49 Domke, supra note 47, at 101.
50 Paul, supra note 4, at 701.
51 Id. at 697-700.
52 Id. at 699.
53 See, e.g., Id. at 702-10.
55 Id. at 2081-82.
ment was intended to affect the Sabbatino case retroactively upon remand. Nevertheless, the court did express perplexity as to whose orders it should follow, those of the Supreme Court or of Congress. The Supreme Court directed application of Act of State, but Congress removed the necessity of its application unless required by the Executive. Generally, mandates of appellate courts are binding on the lower court to which the matter is remanded. However, Congress enacted the legislation with the intention that it should apply to all pending litigation. The Supreme Court has found no denial of constitutional rights when directions of Congress are followed in a lower court after remand from a state appellate tribunal. There is no question that congressional legislation may have a retroactive effect. Banco Nacional de Cuba unsuccessfully pursued this constitutional tack and argued a violation of its constitutional protections under the fifth amendment. The court entertained serious doubts whether the formulators of the Constitution contemplated extension of fifth amendment privileges to foreign states and their representatives. The court explained that the Hickenlooper amendment merely lifted the bar to a consideration of pre-existing questions of substantive rights and liabilities. Therefore, following the dictates of the amendment, the district court delayed final dismissal of the Cuban bank’s complaint for the prescribed period of sixty days from July 30, 1965. The delay afforded the President his statutory opportunity to file a suggestion requesting application of Act of State. As the court stated that unless the President filed a suggestion it would dismiss the complaint, the tribunal must have decided against the Cuban claim upon the merits because the President then failed to file any suggestion requesting application of the Act of State doctrine within the prescribed period.

PROTECTION FOR PRIVATE FOREIGN INVESTORS

It does not appear the Sabbatino (or Farr) case is concluded even though the controversy began more than five years ago. It

56 Id. at 2082.
57 Id. at 2082.
58 Statute cited note 25, supra.
60 Banco Nacional de Cuba v. Farr, supra note 54, at 2082.
61 Ibid.
62 Ibid.
63 Ibid.
could be appealed once more in regard to the latest district court action. All this unending litigation and controversy must leave the prospective United States investor nonplussed. It would appear he must of necessity continue to bear the risk of losing his foreign investment if (1) there is no jurisdiction or the subject matter in controversy cannot be obtained in the courts of developed nations, or (2) if having obtained jurisdiction, the Executive department of the Government determines that application of the Act of State doctrine is in the best interest of the forum state, or (3) given jurisdiction and noninterference by the Executive branch, the seizure is compensated.

In addition, Congress recently has enacted one other program of protection that could be the answer to the plight of many foreign investors.\(^{64}\) The Investment Guaranties program contained in the


"(a) In order to facilitate and increase the participation of private enterprise in furthering the development of the economic resources and productive capacities of less developed friendly countries and areas, the President is authorized to issue guaranties as provided in subsection (b) of this section of investments in connection with projects, including expansion, modernization, or development of existing enterprises, in any friendly country or area with the government of which the President has agreed to institute the guaranty program. The guaranty program authorized by sections 2181-2184 of this title shall be administered under broad criteria, and each project shall be approved by the President."

"(b) The President may issue guaranties to eligible United States investors, or corporations, partnerships, or other associations created under the laws of the United States or of any State or territory and substantially beneficially owned by United States citizens, as well as any wholly-owned (determined without regard to any shares, in aggregate less than 5 per centum of the total of issued and subscribed share capital, required by law to be held by persons other than the parent corporation) foreign subsidiary of any such corporation—

(1) assuring protection in whole or in part against any or all of the following risks:

(A) inability to convert into United States dollars other currencies, or credits in such currencies, received as earnings or profits from the approved project, as repayment or return of the investment herein, in whole or in part, or as compensation for the sale or disposition of all or any part thereof;

(B) loss of investment, in whole or in part, in the approved project due to expropriation or confiscation by action of a foreign government, and

(C) loss due to war, revolution, or insurrection;

Provided, That the total face amount of the guaranties issued under this paragraph (1) outstanding at any one time shall not exceed $5,000,000,000; and

(2) where the President determines such action to be important to the furtherance of the purposes of sections 2181-2184 of this title, assuring against loss of any loan investment for housing projects with appropriate participation by the private investor in the loan risk and in accordance with the foreign and financial policies of the United States, or assuring against
Foreign Assistance Act is intended to relieve, at least partially, expropriation victims who follow the requirements set out by the legislation. The act also is intended to heighten self-development in the developing nations by encouraging private foreign investment. Each project must have presidential approval before the investment is guaranteed against loss, and the investor is insured in whole or in part against expropriation, confiscation, war loss, revolution or insurrection.66 The total amount of guaranty issuable at one time by the President cannot exceed $5,000,000,000.66 One requirement for investment guaranties is that the President must have agreed to institute the program with the country in which an investor seeks to enter commerce.67 Although not all proposed investments can be guaranteed, the program still may aid a large number of concerns previously unwilling to internationalize their operations.68 The Investment Guaranties program is supported and protected to some extent by the Hickenlooper amendment, for which purpose the amendment apparently was intended. The compensation returned to expropriation victims and others by the program acts to subrogate the United States Government as claimant, thus allowing the Government to press a claim in its own behalf against the seizing foreign state.

The Foreign Assistance Act is not the panacea to the problem of expropriation and nationalism nor will any catharsis of confiscation problems present itself in the near future. It is hoped only that the prospective foreign investor now may better understand the problems and risks which originally faced the American investors in the Sabbatino controversy and therefore better protect

loss of not to exceed 75 per centum of any other investment due to such risks as the President may determine, upon such terms and conditions as the President may determine: Provided, That guaranties issued under this paragraph (2) shall emphasize economic development projects furthering social progress and the development of small independent business enterprises: Provided further, That no payment may be made under this paragraph (2) for any loss arising out of fraud or misconduct for which the investor is responsible: Provided further, That the total face amount of the guaranties issued under this paragraph (2) outstanding at any one time shall not exceed $300,000,000, and guaranties issued under this paragraph (2) for other than housing projects similar to those insured by the Federal Housing Administration, shall not exceed $175,000,000: Provided further, That this authority shall continue until June 30, 1987.”

66 Ibid.
66 Ibid.
67 Ibid.
68 Ibid.; for an article on the problems of the Investment Guaranty program, see 64 Colum. L. Rev. 315 (1964).
himself by knowing the probabilities of recovery and the proper avenues in which to channel his claims for compensation in case of loss.⁶⁹

_Larry Lynn Skeen_

⁶⁹ See Foreign Claims Settlement Act 22 U.S.C. § 1622 (1984), explaining the machinery used for foreign claims settlement sought through other than judicial means.