SULLIVAN & CROMWELL LLP

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Second Circuit Rules Creditors Can Require Garnishees to Bring Assets From Abroad to the United States to Satisfy Judgments Against Foreign Sovereigns

In a Noteworthy Ruling for Judgment Creditors, the Second Circuit Held That the Foreign Sovereign Immunities Act Poses No Obstacle to Requiring a Bank in New York to Bring Funds It Holds Outside the United States to New York to Satisfy a Judgment Against Iran

SUMMARY

In *Peterson* v. *Islamic Republic of Iran*, the U.S. Court of Appeals for the Second Circuit became the first court to hold that U.S. courts can compel banks to bring funds held by foreign sovereigns outside the United States to New York to satisfy judgments against those sovereigns. *Peterson* has significant implications for international banks, as the decision will encourage plaintiffs to seek to attach assets held by sovereign judgment debtors at foreign branches of U.S. banks, foreign headquarters of banks with New York branches, and other multinational entities holding foreign assets abroad. That said, the Second Circuit made clear that there are significant prerequisites to forcing banks to bring a foreign sovereign's money from abroad into the United States, which may limit the impact of the opinion.

BACKGROUND

In *Peterson*, victims of Iranian-sponsored terror attacks who hold judgments against Iran sued, among others, JPMorgan Chase Bank, N.A. ("JPMorgan") and Clearstream Banking, S.A. ("Clearstream"), seeking to execute on $1.68 billion in bond proceeds allegedly owned by Bank Markazi, the central bank of Iran. The plaintiffs claimed the funds "were processed by and through a global chain of banks," including Clearstream and JPMorgan.

Clearstream, which is based in Luxembourg, maintained a correspondent account in its name at JPMorgan in New York. When Clearsteam received amounts in the New York account on behalf of Bank Markazi, it would credit Bank Markazi's account, or an account of an intermediary bank, in Luxembourg with a corresponding right to payment. In June 2008, Clearstream blocked the account in Luxembourg, which at that time held $1.68 billion.[1] Plaintiffs in *Peterson* sought, among other things, a declaration that the funds held in the blocked account in Luxembourg belonged to Bank Markazi, rescission of alleged fraudulent conveyances, and a turnover order against JPMorgan and Clearstream.

The U.S. District Court for the Southern District of New York dismissed the complaint, holding with respect to the turnover claims that the assets at issue were not in the United States and that the Foreign Sovereign Immunities Act ("FSIA") "does not allow for attachment of property outside of the United States."[2]

THE SECOND CIRCUIT'S DECISION

In a unanimous decision, the Second Circuit affirmed the holding that the bond proceeds were not held as cash in New York but as a right to payment in Luxembourg.[3] But the Second Circuit reversed the District Court's conclusion that it lacked jurisdiction under the FSIA to order Clearstream to bring the $1.68 billion to the United States to satisfy the judgment against Iran. The Second Circuit's holding was based principally on two precedents, the New York Court of Appeals' decision in *Koehler* v. *Bank of Bermuda Ltd*.[4] and the U.S. Supreme Court's decision in *Republic of Argentina* v. *NML Capital, Ltd.*[5]

In *Koehler*, the New York Court of Appeals (the highest state court in New York) held that under New York State law a court with personal jurisdiction over a garnishee may order the garnishee to bring out-of-state property belonging to a debtor to New York to satisfy a judgment.

In *NML Capital*, the U.S. Supreme Court ruled that the FSIA does not prohibit discovery that a court may order with respect to a sovereign judgment debtor's assets abroad. The Supreme Court's decision rested principally on its conclusion that the FSIA is a comprehensive set of legal standards governing claims of immunity of foreign states and does not provide for any immunity from discovery as such.[6] Argentina argued that the FSIA was not intended to confer authority to execute on assets abroad, and therefore could not have been intended to allow discovery of those assets. Justice Scalia, writing for the Court, rejected that argument, and found that, in fact, the FSIA did not prevent execution on extraterritorial assets. His opinion rested primarily on the text of the immunity-conferring provision of the FSIA, which is limited to "the property *in the United States* of a foreign state."[7]

Noting that state law governs the procedure on execution of judgments in federal court,[8] the Second Circuit in *Peterson* found that "*NML Capital* and *Koehler*, when combined, … authorize a court sitting in New York with personal jurisdiction over a non-sovereign third party to recall to New York extraterritorial assets owned by a foreign sovereign."[9] The Second Circuit remanded the case to the District Court to

determine whether it had personal jurisdiction over Clearstream and, if so, whether there were any other barriers to ordering Clearstream to bring the blocked assets to New York.

IMPLICATIONS

The Second Circuit's conclusion is novel. The Second Circuit distinguished a decision by the U.S. Court of Appeals for the Seventh Circuit (based in Chicago) that had "suggested the contrary conclusion: that even after *NML Capital*, a foreign sovereign's extraterritorial assets remain absolutely immune from execution."[10] As such, *Peterson* is likely to encourage judgment creditors to seek to attach assets held by sovereign judgment debtors at foreign branches of U.S. banks, foreign headquarters of banks with New York branches, and other multinational entities holding foreign assets abroad. That said, there are at least three significant hurdles to the plaintiffs in *Peterson* actually executing on the assets in question, and those hurdles will also apply in many other cases.

Personal jurisdiction. On remand, the District Court in *Peterson* will need to conclude that it has personal jurisdiction—either "general" or "specific"—over Clearstream. A federal district court may exercise general personal jurisdiction over a company if that company's affiliations with the state are so "continuous and systematic" as to render it "essentially at home" in the forum state.[11] The U.S. Supreme Court has said that the "paradig[m] … bases for general jurisdiction" for a corporation are its place of incorporation and principal place of business.[12] If the plaintiffs cannot establish that Clearstream, a company incorporated and headquartered in Luxembourg, is "at home" in New York, they will need to demonstrate specific personal jurisdiction, which requires that Clearstream's conduct in New York gave rise to the plaintiffs' garnishment claims.[13] The plaintiffs will likely argue that the fact that the assets at issue came to rest in Luxembourg after passing through Clearstream's account at JPMorgan in New York provide a sufficient nexus, but it is unclear whether this contact with New York will be sufficient. Thus, the personal jurisdiction requirement may limit the application of *Peterson* largely to entities incorporated or headquartered in New York.

Separate entity doctrine. The separate entity doctrine is a creature of New York law. It "provides that even when a bank garnishee with a New York branch is subject to personal jurisdiction, its other branches are to be treated as separate entities" in garnishment and attachment proceedings.[14] This means that an attachment on a New York branch will not reach assets held by the bank at branches outside of New York. In *Motorola Credit Corp.* v. *Standard Chartered Bank*, the New York Court of Appeals ruled that the separate entity rule survived the court's earlier ruling in *Koehler*.[15] The separate entity doctrine may serve to limit dramatically the use of the *Peterson* doctrine with respect to bank garnishees.

"Commercial activity" and related FSIA requirements. The Second Circuit in *Peterson* also noted that "the FSIA contains several limiting principles" that its opinion did not address, including in most cases that

the assets sought to be attached have been "used for commercial activity in the United States."[16] In an analogous case, the Second Circuit ruled that pension fund assets in New York that Argentina had expropriated and were in New York after expropriation only momentarily as Argentina sought to repatriate them had not been used *by Argentina* for commercial activity while the assets were in New York.[17] Courts may conclude that assets brought into New York by virtue of a court order were not being used by the foreign sovereign for commercial activity in New York.

Chances for certiorari. Given the sensitive question of compelling a bank to bring a foreign sovereign's assets held abroad into the United States, and the arguable "split" in authority between the Second and Seventh Circuits, the U.S. Supreme Court may be open to reviewing the *Peterson* decision. The fact that the case was remanded for further proceedings at the District Court—which may determine on one of the grounds noted above that Clearstream does not need to bring the Iranian assets into the United States—may lessen the Supreme Court's interest in reviewing the case.[18]

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ENDNOTES

1 From 1994 to 2008, Clearstream maintained an account in Luxembourg for Bank Markazi. In January 2008, Bank Markazi instructed Clearstream to transfer its assets to a new account run by Banca UBAE S.p.A. ("UBAE") on Bank Markazi's behalf. Due to increased international scrutiny of Iran's finances, in June 2008 Clearstream suspended UBAE's account and transferred the funds to a frozen account.

2 *Peterson* v. *Islamic Republic of Iran*, No. 13-cv-9195-KBF, 2015 WL 731221, at *10 (S.D.N.Y. Feb. 20, 2015).

3 *Peterson* v. *Islamic Republic of Iran*, No. 15-0690, 2017 WL 5580324, at *14-16 (2d Cir. Nov. 21, 2017).

4 12 N.Y.3d 533, 911 N.E.2d 825, 883 N.Y.S.2d 763 (2009).

5 134 S. Ct. 2250 (2014).

6 134 S. Ct. at 2255-2257.

7 28 U.S.C. § 1609 (*quoted in NML Capital*, 134 S. Ct. at 2256, 2257) (emphasis added).

8 Fed. R. Civ. P. 69(a).

9 2017 WL 5580324, at *20.

10 *Id*. at *21 (citing *Rubin* v. *Islamic Republic of Iran*, 830 F.3d 470 (7th Cir. 2016)).

11 *Daimler AG* v. *Bauman*, 134 S. Ct. 746, 754 (2014) (internal quotation marks and citation omitted).

12 *Id.* at 760 (internal quotation marks and citation omitted).

13 *Helicopteros Nacionales de Colombia, S.A.* v. *Hall*, 466 U.S. 408, 414 n.8 (1984).

14 *Motorola Credit Corp.* v. *Standard Chartered Bank*, 24 N.Y.3d 149, 158, 21 N.E.3d 223, 226 (2014).

15 *Id*.

16 28 U.S.C. §1610(a) (quoted in *Peterson*, 2017 WL 5580324, at *23). The Second Circuit also noted that, to the extent plaintiffs sought to proceed under particular anti-terrorism provisions of the FSIA, they would have to prove that the assets subject to turnover were "blocked," which the court observed was "a term of art imbued with precise meaning." 2017 WL 5580324, at *23.

17 *Aurelius Capital Partners, LP* v. *Republic of Argentina*, 584 F.3d 120, 130-131 (2d Cir. 2009).

18 Stern & Gressman, SUPREME COURT PRACTICE 283 (10th ed. 2017) ("'[E]xcept in extraordinary cases, the writ [of certiorari] is not issued until final decree.' Thus, the lack of finality in the judgement below 'may itself alone' furnish 'sufficient ground for the denial of the application.'") (quoting *Hamilton-Brown Shoe Co.* v. *Wolf Bros. & Co*., 240 U.S. 251, 258 (1916)).

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