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Argentina's Central Bank's Assets in Federal Reserve Account Are Not Subject to Attachment Under the FSIA, Second Circuit Rules

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The author examines a recent decision by the U.S. Court of Appeals for the Second Circuit that ruled that assets held in the United States in an account of non-party Banco Central de la República Argentina at the Federal Reserve Bank of New York were immune from attachment and execution under the Foreign Sovereign Immunities Act of 1976.

The Foreign Sovereign Immunities Act of 1976 ("FSIA")[1] provides the sole basis for obtaining jurisdiction over a foreign state in courts in the United States.[2] The statutory framework for the attachment, arrest, and execution of foreign state property under the FSIA is relatively straightforward. Unless the property of a foreign state, as defined in Section 1603(a),[3] is subject to one of the exceptions set forth in Section 1610, it is immune from attachment, arrest, and execution pursuant to Section 1609.[4] Moreover, even if Section 1610 would otherwise bring foreign state property within the jurisdiction of a court, Section 1611(b)(1)[5] overrides the exceptions in Section 1610,[6] and provides

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that "the property of a foreign state shall be immune from attachment and from execution, if — (1) the property is that of a foreign central bank or monetary authority held for its own account."[7]

Now, in a case in which plaintiffs sought to attach funds held in an account of Banco Central de la República Argentina at the Federal Reserve Bank of New York[8] on the theory that those funds were attachable interests of the Republic of Argentina, the U.S. Court of Appeals for the Second Circuit has held that the plain language, history, and structure of Section 1611(b)(1) immunizes property of a foreign central bank or monetary authority held for its own account without regard to whether the bank or authority is independent from its parent state.

The circuit court's decision, in *NML Capital, Ltd. v. Banco Central de la República Argentina*,[9] helps explain the limits that plaintiffs and judgment creditors face under the FSIA when seeking to attach and execute on funds held in the United States by foreign central banks.

BACKGROUND

The *NML Capital* case arose after the president of the Republic of Argentina declared a temporary moratorium in December 2001 on principal and interest payments on more than $80 billion of public external debt, that is, money that the Republic had borrowed from foreign creditors. Following the 2001 default, Argentina did not make principal or interest payments on its non-performing debt.[10]

EM Ltd. and NML Capital, Ltd., beneficial owners of debt instruments on which the Republic had defaulted, chose not to participate in restructuring proposals in which the Republic offered to exchange debt instruments on which it defaulted in 2001 for new debt instruments with modified, and generally less favorable, terms.[4] Instead, EM and NML Capital sought to recover their investments through litigation against the Republic in the federal courts of the United States.[5] Indeed, they obtained final judgments in the U.S. District Court for the Southern District of New York against the Republic of Argentina for nearly $2.4 billion.[6]

Thereafter, the plaintiffs sought to attach and restrain assets ("FRBNY Funds") held in the United States in an account of non-party Banco Central de la República Argentina ("BCRA") at the Federal Reserve Bank of New York ("FRBNY") in aid of execution of those judgments.

As its name suggests, BCRA was founded in 1935 as the Central Bank of the Argentine Republic. It is, by statute, a self-administered institution of Argentina charged with acting as the Republic's financial agent and as depository and agent for the Republic before international monetary, banking, and financial entities, as well as with regulating the Argentine banking system and financial sector. Pursuant to its primary responsibility to maintain the value of legal tender in Argentina, BCRA is exclusively entrusted with the issuance of banknotes and coins in Argentina and authorized to invest a portion of its external assets in deposits or any other interest bearing transaction with any foreign banking institution.

Like many central banks around the world, BCRA maintains a foreign central bank account at the FRBNY in which, among other things, it manages dollar-denominated reserve holdings.[7] The FRBNY Funds at issue in this case referred to the funds held in BCRA's account on December 30, 2005.

Over the course of the three month period preceding December 30, 2005, BCRA transferred approximately $2.1 billion from its account at the FRBNY to its account at the Bank for International Settlements ("BIS"). This followed a general trend during the period between 2001 and 2005, in which, wholly apart from the intra-day transfers necessary to effect transactions performed out of its FRBNY account, BCRA held more and more of its U.S. dollar-denominated foreign exchange reserves outside of the United States, i.e., beyond the jurisdictional reach of the district court.

This reduction was attributable to two principal causes. First, as economic conditions in Argentina deteriorated leading up to and in the aftermath of the 2001 default, large quantities of U.S. dollars, in excess of $20 billion, were withdrawn from the Argentine banking system. In an

effort to increase liquidity and prevent further economic damage in Argentina, BCRA spent billions of U.S. dollars buying Argentine pesos to defend and prop up the value of the peso. This policy depleted BCRA's dollar-denominated foreign exchange reserves. For example, at the beginning of 2001, BCRA's dollar-denominated international reserves totaled $25.1 billion; two years later the reserves totaled $8.3 billion.

Second, BCRA transferred the majority of its remaining dollar-denominated reserves out of the United States to "more protective jurisdictions," in the view of BCRA, such as the BIS as a preventive measure against possible attachment efforts by creditors of the Republic. BIS deposits are protected from attachment under The Hague Convention of 1930,[11] the Protocol Regarding the Immunities of the Bank for International Settlements,[12] and the Agreement between the Swiss Federal Council and the Bank for International Settlements to determine the bank's legal status in Switzerland.[13] According to the BCRA official responsible for open market operations, in light of temporary attachments by U.S. federal courts, which ultimately were vacated in 1999, the protections offered to BIS account holders were deemed by BCRA to be more secure in circumstances in which an attachment of any significant portion of BCRA's international reserves would quite literally have caused the collapse of the Argentine peso with incalculable effects on the Republic's economy, social order, and political stability.

As a result of the transactional activity in BCRA's account at FRBNY and the transfers out of the FRBNY account to the BIS, at the close of business on December 30, 2005, when the plaintiffs moved to attach the FRBNY Funds, BCRA maintained approximately $105 million in its account at the FRBNY.

The plaintiffs argued that the Republic had consistently disregarded BCRA's independence, thus vitiating any presumption of separateness to which BCRA was entitled and transforming BCRA into an alter-ego of the Republic. Indeed, according to the plaintiffs, the Republic had exploited the legal fiction of that independence unjustly and fraudulently to avoid paying the plaintiffs.

The district court held that the Republic's disregard for BCRA's independence justified the conclusion that BCRA was not entitled to a presumption of juridical separateness and that "[a]s of the end of 2005, when the attachments and restraints in this case were issued, the funds of BCRA were in effect the funds of the Republic."

Second, the district court concluded that although the terms and conditions governing the bonds held by the plaintiffs gave assurances that the rights of the bondholders, that is, the plaintiffs, "may be enforced" in the event of a default, by ensuring that it had no assets within the jurisdiction of the district court, the Republic had created "a path to the judgments, [but with] nothing approaching an accessible path to payment enforcement." Accordingly, the district court held that, with specific regard to the FRBNY Funds, the Republic had perpetrated precisely the sort of "fraud and injustice" that warranted setting aside the presumption of juridical separateness that might otherwise immunize certain funds.

Third, the district court held that the FRBNY Funds were property used for commercial activity in the United States within the meaning of 28 U.S.C. §§1610(a) and (d) because they were used for traditional banking purposes that were clearly "the type of actions by which a private party engages in 'trade and traffic or commerce.'" It therefore did not matter for what purpose BCRA was using the funds, only that the "type of activity," maintenance of a bank account with deposits and withdrawals, with the ability to earn a certain amount of income on balances, was "commercial" in nature.

Finally, the district court held that FSIA Section 1611(b)(1) did not prohibit the attachment of the FRBNY Funds. Although the district court recognized that the FRBNY Funds fell within the explicit terms of Section 1611 because "the account at the FRBNY was in the name of BCRA, and there was no specific waiver of immunity as to this account by BCRA or the Republic," it reasoned that "if there are weighty and sufficient reasons to conclude that the funds in the account were in reality the funds of the Republic, as this court has held, it would be entirely anomalous to hold that the funds belonged to BCRA and were 'held for

its own account,' within the meaning of §1611." In other words, the district court concluded that a determination that the BCRA was not entitled to the presumption of juridical separateness from the Republic overrode the immunity that might otherwise be afforded under Section 1611(b)(1). Accordingly, the district court concluded that the FRBNY Funds were "the property of the Republic," and that "the provisions of the FSIA, when properly applied, permitted [the] attachment[ ] and restraint [of the Funds]."

The Republic and BCRA appealed to the Second Circuit.

THE APPELLATE RULING

As the Second Circuit pointed out, the district court's holding was predicated on the conclusion that immunity under Section 1611(b)(1) was dependent on a central bank's independence. That is, if a central bank lacked sufficient independence to preserve the presumption of juridical separateness, analysis under the FSIA must stop at Section 1610 because the property of the Republic in this case was not entitled to the immunity conferred in §1611(b)(1). As a result, after disregarding the formal separateness of the Republic and BCRA and treating the FRBNY Funds in the hands of BCRA as the funds of the Republic, the district court determined under Section 1610 that (1) the Republic had made the requisite waivers of immunity as to its property, which included the FRBNY Funds, and (2) the FRBNY Funds should be considered property of the Republic used for commercial activity in the United States. The district court declined to conduct an analysis of the FRBNY Funds' immunity under Section 1611 because "the [FRBNY Funds were] in fact not the property of BCRA held for its own account, but [were] the property of the Republic."

The circuit court decided that the district court had misread the FSIA when it concluded that a court facing the question of whether the assets of a central bank were attachable property under the FSIA first must decide whether the central bank was entitled to a presumption of indepen-

dence from its parent state. The Second Circuit then held that the plain language, history, and structure of Section 1611(b)(1) immunized property of a foreign central bank or monetary authority held for its own account without regard to whether the bank or authority was independent from its parent state. If foreign central bank property was immune from attachment under Section 1611(b)(1), the fact that a relationship of principal and agent had been created between the foreign state and its central bank was "irrelevant," according to the circuit court. It then stated that foreign central banks are not treated as generic "agencies and instrumentalities" of a foreign state under the FSIA; they are given "special protections" befitting the particular sovereign interest in preventing the attachment and execution of central bank property. In the opinion of the Second Circuit, the plaintiffs could not evade this statutory requirement to turn assets that otherwise would be considered property of a central bank held for its own account into property of the Republic that was not entitled to immunity.

The Second Circuit observed that the text of the statute provides that the only qualification for immunity under Section 1611(b)(1) was whether the property of the central bank was "held for its own account." It then noted that the law's language suggested that Congress recognized that the property of a central bank, immune under Section 1611, also might be the property of that central bank's parent state. The circuit court pointed out that the federal government, appearing as amicus curiae, had stated, "if Congress had intended to limit §1611(b)(1) to independent central banks, one would have expected the introductory language of the subsection — 'Notwithstanding the provisions of section 1610 of this chapter' — to refer only to §1610(b), which provides for execution or attachment of the property of state agencies and instrumentalities, rather than to §1610 as a whole." Section 1611(b)(1), however, referred to Section 1610 in its entirety, including those provisions of Section 1610 applicable only to foreign states. Therefore, according to the Second Circuit, the statute seemed to anticipate the possibility that property held by a central bank also might be property of a sovereign state.

The Second Circuit explained that the plaintiffs contended that when

Congress chose to immunize the "property of a foreign central bank," it had in mind the property of a government agency or instrumentality with "separate legal personhood." The Second Circuit rejected that view, however, explaining that in the House Report on the FSIA, Congress explained that:

> Section 1611(b)(1) provides for the immunity of central bank funds from attachment or execution. It applies to funds of a foreign central bank or monetary authority which are deposited in the United States and "held" for the bank's or authority's "own account" — i.e., funds used or held in connection with central banking activities, as distinguished from funds used solely to finance the commercial transactions of other entities or of foreign states. If execution could be levied on such funds without an explicit waiver, deposit of foreign funds in the United States might be discouraged. Moreover, execution against the reserves of foreign states could cause significant foreign relations problems.[14]

As the circuit court noted, the FSIA House Report reflected Congress's understanding that although the funds of foreign central banks were managed through those banks' accounts in the United States, those funds were, in fact, the reserves of the foreign states themselves.[15] In other words, it continued, the property of central banks deserved protection notwithstanding the fact that central banks might not have separate legal personhood. By referring to the property of a foreign state and the property of a central bank interchangeably, Congress indicated its understanding that central bank property could be viewed as the property of a foreign state, and nonetheless be immune from attachment, the Second Circuit stated.

The most convincing argument in favor of this interpretation, the Second Circuit said, was that the historical backdrop against which the FSIA was passed foreclosed the argument that a determination of agency liability could render property attachable that was otherwise immune under Section 1611(b)(1). In the 1970s, when Congress passed the FSIA, it had

no reason to believe that foreign central banks and monetary authorities would be independent of their parent states because, at that time, most were not.

Moreover, the circuit court continued, Congress had reason to suspect that, as appeared to be the case with Argentina, a central bank's actual degree of autonomy might not be entirely predictable based on its degree of juridical independence. In an environment in which Congress was worried that execution against foreign central bank deposits might "discourage[]" foreign states from depositing their reserves in the United States,[16] it made "no sense" to assume that Congress would enact a statute designed to prevent "significant foreign relations problems" that failed to immunize a significant portion of the central bank reserves in the United States at that time.

Thus, the Second Circuit concluded, Section 1611(b)(1) immunizes foreign central bank property "held for its own account" without regard to the central bank's independence from its parent state; that is, the appellate court held that the analysis of the immunity of a foreign central bank's property begins with Section 1611(b)(1). The appellate court added that there was no indication in the text, history, or structure of the FSIA that Congress intended to make the immunity of a central bank's property contingent on the independence of the central bank. The statute made "no reference to the independence or autonomy of a central bank or monetary authority." Moreover, the history of the FSIA and of the independence of central banks suggested that Congress understood the property of a foreign central bank to be deserving of immunity "regardless of that bank's independence." The Second Circuit ruled that the plaintiffs had failed to convince it that an independence requirement could be fairly read into the statute.

APPLICATION TO FRBNY FUNDS

Having concluded that the immunity of the FRBNY Funds under the FSIA turned not on whether the BCRA was entitled to a presumption of

independence from the Republic, but on whether the funds were property of the BCRA "held for its own account" under Section 1611(b)(1), the Second Circuit then had to decide whether the FRBNY Funds met that test.

The definition of the phrase "held for its own account" in Section 1611(b)(1) was a matter of first impression in the Second Circuit. The parties suggested three different ways the circuit court could interpret that phrase.

First, BCRA argued that central bank property was "held for its own account" if that property was used for "traditional central banking activities." The circuit court noted that this appeared to be the test adopted by Congress in the FSIA,[17] and apparently was the only test ever to be applied by a federal court in this country.[18]

The FRBNY, as amicus curiae, offered a second proposed definition of central bank property "held for its own account." It suggested an alternative definition drawn from the common law of bank deposits. Under the so-called "plain language test," property of a central bank was "held for its own account" if it was in an account in the central bank's name because "[u]nder fundamental banking law principles, a positive balance in a bank account reflected a debt from the bank to the depositor" and no one else.

Finally, relying on a "grammatical and syntactical construction of Section 1611(b)," the plaintiffs suggested a third definition of property of a central bank "held for its account": "[p]roperty of a central bank is 'held for its own account' when it is held for [the central bank's] own profit or advantage." According to the plaintiffs, in the statutory phrase "property … of a foreign central bank held for its own account": (1) the words "its own" referred back to the term "central bank" (not "property"), and (2) the word "for" denoted that the words that followed — "its own account" — constituted the purpose for which the property was "held." The plaintiffs argued that if a court were to disregard the juridical separateness of BCRA, the FRBNY Funds could not be held for the central bank's own profit or advantage because the central bank was the sovereign.

The Second Circuit decided that the plaintiffs' definition was "nov-

el" but that it could not be correct. It noted that BCRA was charged by statute with power and responsibility over, among other things, issuing and monitoring the stability of the Argentine peso, establishing and implementing monetary policy, investing reserves, acting as the Republic's financial agent and as depository and agent for the Republic before "international monetary, banking and financial entities," and regulating the Argentine banking system and financial sector. These all were traditional activities of central banks that were performed "in the national economic interest." They also were functions that defied any attempt to divide the interest of the central bank from that of the state it served.

The circuit court continued by noting that the plaintiffs offered no standard for deciding whether a given reserve policy or central bank investment was conducted for the "advantage" of the central bank or that of its parent state. It suspected that the plaintiffs did not offer a standard because "no reasonable strategy" existed. Indeed, it pointed out, BCRA's charter made explicit that at the end of each year BCRA's "profits," above and beyond 50 percent of its capital, were required by law to "be freely transferred to the National Government account." The Second Circuit also stated that, notwithstanding the BCRA's independent legal status, asking courts to disaggregate activities that were for BCRA's advantage and not the Republic's (or vice versa) misunderstood the legal structure of BCRA and the very purpose of a central bank.

On the other hand, the Second Circuit stated, the "central banking activities" test was not without difficulty, either. On its face, the House Report distinguished between property "used or held in connection with central banking activities," which was immune from attachment under Section 1611(b)(1), and that used "solely to finance the commercial transactions … of foreign states," which was not.[19] However, according to the Second Circuit, the structure of the FSIA suggested that property used for commercial activity and property of a central bank held for its own account were not mutually exclusive categories, because some property of a central bank held for its own account was a category of property used for commercial activity.

The Second Circuit then adopted a "modified central bank functions test," pursuant to which property of a central bank was immune from attachment if the central bank used the property for central banking functions as such functions were normally understood, irrespective of their commercial nature." Conversely, the circuit court continued, if an activity was to be regarded as commercial, as distinguished from a central bank activity, it should be an activity of the foreign central bank not generally regarded as a central banking activity.[20]

In the circuit court's view, this modified test, which combined the "plain language" of the statute and "central bank activities" tests as conjunctive requirements, accorded with the text and purpose of Section 1611(b)(1), and it therefore adopted this test for purposes of determining whether central bank property was "held for its own account." Where funds were held in an account in the name of a central bank or monetary authority, the funds were presumed to be immune from attachment under Section 1611(b)(1). A plaintiff, however, could rebut that presumption by demonstrating with specificity that the funds were not being used for central banking functions as such functions were normally understood, irrespective of their "commercial" nature.

The Second Circuit then stated that, had the district court applied this test, it would have concluded that the FRBNY Funds were property of the BCRA held for the central bank's own account at FRBNY. It noted that the FRBNY Funds were held in BCRA's name at FRBNY, adding that the record clearly established that the accumulation of foreign exchange reserves to facilitate the regulation of the peso and the custody of cash reserves of commercial banks pursuant to central bank regulations were paradigmatic central banking functions.

The Second Circuit concluded by indicating that it understood "the frustration" of plaintiffs who were attempting to recover on judgments they had secured. Nevertheless, it said, it had to respect the FSIA's "strict limitations on attaching and executing upon assets of a foreign state." Accordingly, it held that the FRBNY Funds were immune from attachment and restraint.

CONCLUSION

The Second Circuit's decision that assets held in the United States in an account of non-party Banco Central de la República Argentina at the Federal Reserve Bank of New York are immune from attachment and execution under the FSIA is an important creditors' rights decision just as it is an important international relations ruling. The circuit court recognized that its opinion puts creditors in a difficult position, but unless Congress changes the law, this very well may be the final word on the issue.

NOTES

[1] 28 U.S.C. §§1602 et seq.

[2] *Argentine Republic v. Amerada Hess Shipping Corp*., 488 U.S. 428 (1989).

[3] FSIA Section 1603(a)-(b) provides that:

> (a) [a] "foreign state," except as used in section 1608 of this title, includes a political subdivision of a foreign state or an agency or instrumentality of a foreign state as defined in subsection (b).
>
> (b) An "agency or instrumentality of a foreign state" means any entity —
>
> (1) which is a separate legal person, corporate or otherwise, and
>
> (2) which is an organ of a foreign state or political subdivision thereof, or a majority of whose shares or other ownership interest is owned by a foreign state or political subdivision thereof, and
>
> (3) which is neither a citizen of a State of the United States as defined in section 1332(c) and (e) of this title, nor created under the laws of any third country.

[4] FSIA Section1609 provides, in full, that "[s]ubject to existing international agreements to which the United States is a party at the time of enactment of this Act[,] the property in the United States of a foreign state shall be immune from attachment[,] arrest[,] and execution except as provided in sections 1610 and 1611 of this chapter."

[5] FSIA Section 1611(b) provides, in full, that:

> (b) Notwithstanding the provisions of section 1610 of this chapter, the property of a foreign state shall be immune from attachment and from

execution, if —

(1) the property is that of a foreign central bank or monetary authority held for its own account, unless such bank or authority, or its parent foreign government, has explicitly waived its immunity from attachment in aid of execution, or from execution, notwithstanding any withdrawal of the waiver which the bank, authority or government may purport to effect except in accordance with the terms of the waiver; or

(2) the property is, or is intended to be, used in connection with a military activity and

(A) is of a military character, or

(B) is under the control of a military authority or defense agency.

[6] *See Banque Compafina v. Banco de Guatemala*, 583 F. Supp. 320 (S.D.N.Y. 1984).

[7] 28 U.S.C. §1611(b)(i); *see generally De Letelier v. Republic of Chile*, 748 F.2d 790 (2d Cir. 1984) ("[U]nder [FSIA] §1609 foreign states are immune from execution upon judgments obtained against them, unless an exception set forth in §§1610 or 1611 of the FSIA applies.").

[8] The FRBNY provides accounts in which approximately 250 foreign central banks and monetary authorities manage foreign exchange reserve holdings and other property. As of December 31, 2009, the balances in these accounts totaled nearly $3 trillion, representing more than half of the worldwide U.S. dollar-denominated reserves.

[9] 10-1487-cv(L) (2d Cir. July 5, 2011).

[10] The Republic had waived its right to assert its sovereign immunity from suit in any claims arising under those instruments.

[11] 104 L.N.T.S. 441 (Jan. 20, 1930) (available at http://www.bis.org/about/convention-en.pdf) (establishing the BIS).

[12] 197 L.N.T.S. 31 (July 30, 1936) (available at http://www.bis.org/about/protoc.pdf).

[13] Feb. 10, 1987, amended Jan. 1, 2003 (available at http://www.bis.org/about/headquart-en.pdf).

[14] FSIA House Report 31, *reprinted in* 1976 U.S.C.C.A.N. 6604 at 6630.

[15] *Id.*

[16] *See id.*

[17] *See* FSIA House Report 31, reprinted in 1976 U.S.C.C.A.N. at 6630 (Funds "'held' for the bank's or authority's 'own account' … [include] funds used or held in connection with central banking activities, as distinguished

from funds used solely to finance the commercial transactions of other entities or of foreign states").

[18] *See, e.g., Ministry of Def. & Support for Armed Forces of Islamic Repub. of Iran v. Cubic Def. Sys*., 385 F.3d 1206, 1223-24 (9th Cir. 2004) (discussing FSIA House Report for the proposition that "held for its own account" means "used or held in connection with central banking activities"), *vacated on other grounds sub nom., Ministry of Def. & Support for Armed Forces of Islamic Repub. of Iran v. Elahi*, 546 U.S. 450 (2006); *Bank of Credit and Commerce Int'l (Overseas) Ltd. v. State Bank of Pak*., 46 F. Supp. 2d 231 (S.D.N.Y. 1999) ("Pursuant to 28 U.S.C. §1611, the property of a foreign central bank held 'for its own account' is immune from attachment in the United States. Funds are considered to be 'held for a central bank's own account' if they are used to perform functions that are normally understood to be the functions of a nation's central bank, and are not utilized in commercial activities."), *vacated on other grounds*, 273 F.3d 241 (2d Cir. 2001); *Banco Central de Reserva del Peru v. Riggs Nat'l Bank of Washington, D.C*., 919 F. Supp. 13 (D.D.C. 1994) (citing FSIA House Report); *Banque Compafina v. Banco de Guatemala*, 583 F. Supp. 320 (S.D.N.Y. 1984) (same).

[19] FSIA House Report 31, reprinted in 1976 U.S.C.C.A.N. at 6630.

[20] *See* Ernest T. Patrikis, "Foreign Central Bank Property: Immunity from Attachment in the United States," 1982 U. Ill. L. Rev. 265 (1982).