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Client Alert

Business Litigation Practice Group

October 3, 2012

Second Circuit Rules that a Judgment-Creditor is Entitled to Broad Discovery Concerning Foreign State Judgment-Debtor's Assets

On August 20, 2012, the United States Court of Appeals for the Second Circuit issued its ruling in *EM Ltd. v. Republic of Argentina*,[i] which clarifies the scope of protection afforded to foreign states and their instrumentalities under the Foreign Sovereign Immunities Act (FSIA) in connection with post-judgment enforcement proceedings. The decision, which held that a party that has obtained a valid judgment against a foreign state is entitled to broad post-judgment discovery concerning the foreign state's assets located both within the United States and abroad, re-affirmed existing Second Circuit precedent establishing a court's authority to order post-judgment discovery against foreign states in aid of enforcement, and expressly disagreed with a recent ruling of the Seventh Circuit which found that a district court's power to order post-judgment discovery into a foreign state's assets was much more strictly limited under the FSIA.[ii] The Second Circuit's decision provides considerable aid to judgment-creditors holding judgments against foreign states, and moves the Second Circuit's FSIA-jurisprudence further toward reconciling the tension between respecting the sovereignty of foreign nations who are hauled into U.S. courts by affording parties holding judgments against foreign states a meaningful ability to enforce those judgments, particularly judgments against foreign states who have made a pre-dispute contractual waiver of sovereign immunity, but nonetheless continued to invoke it as an impediment to satisfying a duly-rendered U.S. court judgment.

Background

The EM Ltd./NML Capital, Ltd. dispute with Argentina arises out of Argentina's December 2001 default on its sovereign debt instruments, an event which has generated nearly nine years of litigation in the Southern District of New York and has produced a litany of decisions from the Court of Appeals.[iii] EM Ltd. and NML Capital, Ltd. (NML) are both holders of Argentinean debt and sought to recover funds due

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on the defaulted bonds in the U.S. District Court for the Southern District of New York. Five money judgments were entered in NML's favor against Argentina in the total amount of approximately $1.6 billion with interest. The district court also granted summary judgment to NML in six additional actions, in which NML's claims totaled (with interest) more than $900 million. In its efforts to enforce those judgments, NML sought discovery into the location of Argentina's assets. NML served third party subpoenas on banks in the U.S. and abroad seeking information concerning "Argentina's assets and accounts . . . how Argentina moves its assets through New York and around the world, and . . . the places and times when those assets might be subject to attachment and execution (whether under [U.S. law] or the law of foreign jurisdictions)" (the "Subpoenas"). Specifically, the Subpoenas sought production of, *inter alia*, "documents sufficient to identify the opening and closing dates of Argentina's accounts, current balances and transaction histories from 2009 through the production date," as well as "documents relating to electronic fund transfers sent through the SWIFT system." The Subpoenas defined "Argentina" broadly to include Argentina's "agencies, ministries, instrumentalities, political subdivisions, employees, attorneys, representatives, affiliates, subsidiaries, predecessors, successors, alter-egos, and assigns, and all other Persons acting or purporting to act for or on Argentina's behalf, whether or not authorized to do so." The Subpoenas further set forth a list of past and current government officials and state-owned corporations to be included within the definition of "Argentina."

Argentina and one of the banks that received a Subpoena moved to quash the Subpoena, while NML cross-moved to compel compliance.[iv] The district court denied the motion to quash and granted the motions to compel. Determining that extraterritorial asset discovery did not infringe on Argentina's sovereign immunity, the district court stated that it intended to serve as a "clearinghouse for information" in NML's efforts to find and attach Argentina's assets.

Argentina appealed the district court's order compelling the banks to comply with the Subpoenas. Argentina argued that the Subpoenas, which ordered the production of information concerning Argentina's assets located outside of the United States, violated its sovereign immunity under the FSIA. Specifically, Argentina claimed that because the FSIA only permits a U.S. court to execute assets located in the United States, the FSIA prohibits discovery concerning assets outside the United States. The Court of Appeals was thus asked to consider the "scope of discovery available to a plaintiff in possession of a valid money judgment against a foreign sovereign." *Id.* at *1.

The Court of Appeals' Rulings

The Court of Appeals held that the Subpoenas could be enforced. Central to the Court of Appeals' ruling was its finding that a judgment creditor's right to obtain discovery over a sovereign judgment-debtor's assets is not derived from, and is therefore not limited by, the FSIA. The Court anchored its decision in the well-established principles that "[a] district court has broad latitude to determine the scope of discovery and to manage the discovery process," and that "broad post-judgment discovery in aid of execution is the norm in federal and New York state courts," subject of course, to the courts' "broad discretion to limit discovery in a prudential and proportionate way." *Id.* at *4. Further, the Court noted that "in a run-of-the-mill execution

proceeding," a judgment creditor would be permitted to seek discovery into assets located outside the jurisdiction of the court where the discovery request is made. *Id.*

As noted above, Argentina had asserted that the normal rule of broad discovery in aid of execution must be limited by principles of sovereign immunity, and that because its property located abroad was categorically immune from attachment by a U.S. court, the district court was not permitted to order discovery into those assets. The Court flatly rejected that argument. It noted first that the "question of whether the FSIA extends immunity to property held outside the United States" remains unanswered. While recognizing that "a district court sitting in Manhattan does not have the power to attach Argentinean property in foreign countries," the Court explained that, under its prior precedent, "the district court's power to order discovery to enforce its judgment does not derive from its ultimate ability to attach the property in question but from its power to conduct supplementary proceedings, involving persons indisputably within its jurisdiction to enforce valid judgments." *Id.* at *5 (citing *First City, Texas-Houston, N.A. v. Rafidain Bank*, 281 F.3d 48 (2d Cir. 2002)).[v] In sum, the Court of Appeals held unequivocally that:

> **[w]hether a particular sovereign asset is immune from attachment must be determined separately under the FSIA, but this determination does not affect discovery**. Whatever hurdles NML will face abroad before ultimately attaching Argentina's property abroad (and we have no doubt there will be some), it need not satisfy the stringent requirements for attachment in order to simply receive information about Argentina's assets.

Id. (emphasis supplied). Thus, the Court held that "the Discovery Order does not implicate Argentina's immunity from attachment under the FSIA. It does not allow NML to attach Argentina's property, or indeed have any effect on Argentina's property at all; it simply mandates [the Banks'] compliance with *subpoenas duces tecum*." *Id.* at *5 (emphasis supplied).

The Court made note of another decision from the Court of Appeals for the Seventh Circuit, *Rubin v. Islamic Republic of Iran*, 637 F.3d 783 (7th Cir. 2011), in which that court reached a different conclusion concerning the scope of the FSIA's limitations on post-judgment discovery in holding that the FSIA requires a judgment creditor to identify specific non-immune assets before it is entitled to further discovery about those assets. The Court of Appeals for the Second Circuit expressly declined to follow *Rubin*, noting:

> We respectfully disagree with the the Seventh Circuit to the extent it concluded that the district court's subject matter jurisdiction over a foreign sovereign was insufficient to confer the power to order discovery from a person subject to the court's jurisdiction that is relevant to enforcing a judgment against the sovereign. Such a result is not required by the FSIA and is in conflict with our holding in *Rafidain II* that a district court's jurisdiction over a foreign sovereign extends to proceedings to enforce a valid judgment.

Id. at *6.

The Court of Appeals further explained that, to the extent any that the discovery order could even arguably have implicated an immunity conferred by the FSIA, it would have been Argentina's immunity from the district court's subject matter and *in personam* jurisdiction. However, Argentina had expressly waived any such immunity in the underlying bond agreements. Since it was indisputable that the district court possessed both subject matter jurisdiction over the case and personal jurisdiction over Argentina, there was no question that the district court was authorized to order discovery designed to aid in enforcing its judgments. *Id.* Specifically, the Court of Appeals held that Argentina's waiver of sovereign immunity left it largely in the same position with respect to discovery as a non-sovereign party who is subject to the Court's jurisdiction:

> Once the district court had subject matter and personal jurisdiction over Argentina, **it could exercise its judicial power over Argentina as over any other party**, including ordering third-party compliance with the disclosure requirements of the Federal Rules.

Id. at *6 (emphasis supplied).

The Court of Appeals noted the important distinction between discovery requests made before a court conclusively has jurisdiction over a foreign sovereign and those made after jurisdiction has been established. The Court explained that sovereign immunity protects a sovereign from the "expense, intrusiveness, and hassle of litigation" and requires that discovery be ordered "circumspectly" only where the court's jurisdiction over the foreign sovereign has not yet been established. However, where jurisdiction has already been established, "the concerns voiced in *Rafidain II* are not present, and our precedents relating to jurisdictional discovery are inapplicable." *Id.*

Finally, the Court explained that a "second principal reason" that the discovery order could not be said to infringe upon Argentina's sovereign immunity was that the subpoenas at issue were directed at banks, not Argentina. As none of those banks were entitled to sovereign immunity, and their compliance with the Subpoenas would not cause Argentina any burden or expense, Argentina essentially lacked standing to claim that the discovery order violated the FSIA. The Court noted that Argentina's concerns about the banks' disclosure of privileged information were adequately addressed under the Federal Rules, and that the protection of sensitive or otherwise confidential information could be addressed with an appropriate confidentiality agreement. *Id.* at *7.

Conclusions

The *EM Ltd.* decision provides much-needed clarification on the precise contours of the different immunities conferred by the FSIA. While the Court did not purport to expand the holdings of its decision in *Rafidain*, its analysis more clearly defined the powers of a district court under the jurisdictional provisions of the FSIA,

which in a sense were rendered toothless under the Seventh Circuit's analysis decision in *Rubin*. Although the Second Circuit has previously recognized that "the FSIA reflects a deliberate congressional choice to create a 'right without a remedy' in circumstances where there is jurisdiction over a foreign state for purposes of obtaining a judgment, but its property is immune from attempts to execute the judgment,"[vi] the *EM Ltd.* decision makes clear that a U.S. court that validly exercises its jurisdiction under the FSIA to render a judgment against a foreign state is not completely powerless to aid the judgment-creditor. After all, broad disclosure requirements are a hallmark of U.S. litigation, and asset discovery is a powerful tool for judgment-creditors left in the position of having to enforce their own judgment. The Court's decision appears to reflect an inherent understanding that enforcing a judgment against a foreign state often requires a multijurisdictional effort, and that while U.S. courts may have limitations on their ability to exercise jurisdiction over assets located outside of the United States, they can serve as a "clearinghouse" of information that might be relevant to the judgment-creditor's global efforts to collect on its judgment.

Perhaps the most interesting statement by the Court of Appeals in the *EM Ltd.* decision was that the "question of whether the FSIA extends immunity to property held outside the United States" was yet unanswered in the Second Circuit. While not directly at issue in the case, the *EM Ltd.* decision made that question even more important in light of recent New York state court decisions holding that a court with personal jurisdiction over a third-party garnishee is authorized to direct that judgment-debtor or garnishee to deliver money or property located outside of New York into New York for purposes of satisfying a judgment. *See, e.g., Koehler v. Bank of Bermuda*, 12 N.Y.3d 533, 537, 883 N.Y.S.2d 763, 766 (2009) (explaining that the "turnover" remedy provided for in N.Y. C.P.L.R. § 5225 operates based on jurisdiction over the person, and ruling as a matter of New York law that a court may order a judgment-debtor or garnishee over whom it has personal jurisdiction to deliver property to a judgment creditor in aid of a judgment, since such an order necessarily does not involve any exercise of jurisdiction over the property itself); *see also Hotel 71 Mezz Lender LLC v. Falor*, 14 N.Y.3d 303, 310, 900 N.Y.S.2d 698, 702-03 (2010) (noting that "a court with personal jurisdiction over a nondomiciliary present in New York has jurisdiction over that individual's tangible or intangible property, even if the situs of the property is outside New York," and affirming pre-judgment attachment of defendant's interests in various limited liability companies located outside of New York). The Court of Appeals' decision in *EM Ltd.* focused, like the New York Court of Appeals in *Koehler* and *Hotel 71 Mezz*, on the fundamental difference between exercises of *in personam* jurisdiction over parties and *in rem* jurisdiction over property, and its analysis appears to recognize that the FSIA's "execution immunity"—which provides that "the property in the United States of a foreign state shall be immune from attachment arrest and execution," subject to contrary international law and various exceptions[vii]—does not automatically apply to all post-judgment enforcement proceedings, but only to attempts to assert *in rem* jurisdiction over "the property of a foreign state" by "attaching, arresting, and/or executing" that property.

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[i] ___ F.3d ___, 2012 WL 3553367 (2d Cir. Aug. 20, 2012).

[ii] *See Rubin v. Islamic Republic of Iran*, 637 F.3d 783 (7th Cir. 2011).

[iii] *See, e.g.*, *NML Capital, Ltd. v. Republic of Argentina*, 680 F.3d 254 (2d Cir. 2012); *NML Capital, Ltd. v. Banco Central de la Republica Argentina*, 652 F.3d 172 (2d Cir. 2011); *Aurelius Capital Partners, LP v. Republic of Argentina*, 379 Fed. Appx. 74 (2d Cir. 2010); *EM Ltd. v. Republic of Argentina*, 389 Fed. Appx. 38 (2d Cir. 2010); *Aurelius Capital Partners, LP v. Republic of Argentina*, 584 F.3d 120 (2d Cir. 2009); *Seijas v. Republic of Argentina*, 352 Fed. Appx. 519 (2d Cir. 2009); *Mazzini v. Republic of Argentina*, 282 Fed. Appx. 907 (2d Cir. 2008); *Fontana v. Republic of Argentin*a, 415 F.3d 238 (2d Cir. 2005); *EM Ltd. v. Republic of Argentina*, 131 Fed. Appx. 745 (2d Cir. 2005); *EM Ltd. v. Republic of Argentina*, 382 F.3d 291 (2d Cir. 2004).

[iv] Prior to the District Court's rulings on the objections, NML agreed to modify the Subpoenas by excluding lower-level Argentinian officials from searches of SWIFT messages, and by entering into a protective order covering all documents designated by the banks as confidential.

[v] In *First City*, plaintiff First City, Texas-Houston, N.A. ("First City") sought to collect on a defaulted letters of credit issued by Rafidain Bank ("Rafidain"), Iraq's state-owned commercial bank. First City obtained a default judgment against Rafidain, and sought to collect that judgment from the Central Bank of Iraq ("Central Bank") on the theory that Central Bank was Rafidain's alter ego. Rafidain appealed a discovery order entered by the district court directing Rafidain's compliance with discovery requests concerning the alter ego question. Rafidain appealed the order on the grounds that the district court lacked personal and subject matter jurisdiction because, "even if the FSIA afforded jurisdiction in the underlying litigation involving a loan agreement and letters of credit, Rafidain is no longer a party to that action and there is no alternative jurisdictional basis for compelling Rafidain to submit to non-party discovery in the United States." *Id.* at 51. The district court disagreed, concluding that "where subject matter jurisdiction under the FSIA exists to decide a case, jurisdiction continues long enough to allow proceedings in aid of any money judgment that is rendered in the case. In this case, that includes discovery regarding a possible alter ego of Rafidain that may have assets sufficient to satisfy First City's judgment." *Id.* at 54.

[vi] *Walters v. Industrial and Commercial Bank of China, Ltd.*, 651 F.3d 280, 289 (2d Cir. 2011) (citing *De Letelier v. Republic of Chile*, 748 F.2d 790, 799 (2d Cir. 1984)).

[vii] See 28 U.S.C. §§ 1609-1611.