In another hemisphere: state immunity in Jersey and elsewhere since FG Hemisphere Associates LLC

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The mere fact of being owned by a sovereign state does not give a Jersey company "sovereign immunity" from legal proceedings. As a result, creditors can sue and enforce against a state-owned company's assets, including strategically important assets (such as oil pipeline companies) to obtain payment. In the Jersey case of *FG Hemisphere Associates LLC* the Privy Council held that a state's debts could not be enforced against companies owned by that state. In *Tepe Insat Sanayii AS v Boru Hatlari Ile Petrol Tasima AS (Botas) [2016] JRC 012A*, the Royal Court has now considered the reverse question: can state-owned companies avoid liability by claiming state immunity from legal proceedings? In answering "no", the Court held there are two different types of state immunities: immunity from suit prior to judgment, and immunity from enforcement of a judgment obtained. At the same time, the High Court of Australia separately made the same distinction. Surprisingly, applying this distinction Jersey's Court held an application to enforce an arbitration award in which a company claimed state immunity involved immunity from suit, rather than immunity from enforcement.

Background

The issue arose from an unpaid bill. Tepe was a Turkish construction company. Botas was a Turkish oil company owned by the Republic of Turkey. Botas employed Tepe to construct facilities on sections of the Baku-Tblisi-Ceyhan oil pipeline which transports petroleum from Azerbaijan to the Mediterranean.

Botas refused to pay, so Tepe took it to ICC arbitration, and won. As Botas still refused to pay, Tepe sought to enforce the awards by arresting Botas' assets. These included wholly owned subsidiary companies registered in Jersey: BIL, the operator of the BTC pipeline, and TPIC, Botas' principal operational E&P arm exploring and producing petroleum throughout Turkey, the Middle East, Russia and central Asia, and Latin America.

Tepe applied to register the awards under Jersey's applicable arbitration legislation. At the same time it applied for an arrêt – a traditional Jersey remedy (Guernsey has one similar) - to arrest Botas' shares to satisfy the awards.

The issue

Botas objected that it was wholly owned by the Turkish state, and so its wholly owned assets, BIL and TPIC, were entitled to sovereign immunity from enforcement.

The Court rejected this argument. Whilst Botas was owned by Turkey, it was not the state itself.

This begged the question how it could claim sovereign immunity.

Basis and types of sovereign immunity

Sovereign immunity is governed by statute in Jersey, which adopted the English State Immunity Act 1978. This provides that states are immune from court action, subject to certain exceptions. The Act contained two sets of similar-looking provisions potentially relevant to Tepe's case.

- First, the Act provides that the Court could entertain proceedings against a person other than a state, notwithstanding that the proceedings relate to property in the possession or control of a state or in which it claims an interest, if the state itself would not have been immune. Relevant exceptions to the state's immunity for these purposes included that the proceedings related to a commercial transaction.
- Secondly, it provides that an entity separate to the state is immune if, and only if, the proceedings relate to anything done by it in the exercise of sovereign authority and the state would have been immune. Although this appears duplicative of the first provisions above, the Court held it must be read with a further provision that property of a state shall not be subject to any enforcement of a judgment or arbitration award. This provision is subject to a further exception that it does not apply to property currently used or intended to be used for commercial purposes.

So, what was the significance of these differing provisions and how do they relate to each other? The Royal Court held they related to different parts of legal proceedings:

- The first provisions give immunity from suit in ordinary court proceedings in which the parties ask the Court to adjudicate and give judgment on a dispute (such as the right to be paid the contracted price) ("adjudicative immunity").
- The second provisions give immunity from enforcement proceedings, the next step where a party, if still unpaid, takes further action to force or obtain the payment the Court has now adjudged him or her entitled to ("enforcement immunity").

Meanwhile, in another hemisphere

While the Jersey Court was considering its judgment, a funds case was being heard in Australia which mirrored some of the Jersey Court's reasoning and distinction between adjudicative and enforcement immunities.

Firebird Global Master Fund II Ltd v Republic of Nauru [2015] HCA 43 concerned a fund, Firebird, holding bonds issued by a Nauru statutory corporation. The Republic of Nauru guaranteed those bonds. The corporation defaulted, so Firebird sued Nauru to judgment in Japan. It then sought to register that judgment and enforce it in Australia where Nauru held bank accounts.

The Australian Court:

- Explained the adjudicative immunity as applying to that adjudicative jurisdiction, which meant any application to the court in its civil jurisdiction for its intervention or action, or moving a court to do something according to the law.
- Decided that an application to register a judgment was not merely enforcement, it was an application to the Court to decide whether or not to enter an Australian judgment matching the foreign one, and so create new rights in Australia. It was therefore adjudicative.
- Held that a consequent application to exercise the new rights obtained and attach Nauru's assets in Australia engaged the second, enforcement immunity.

Which immunity applied

Which immunity potentially applied to Botas? The answer is surprising. Tepe was applying to register and enforce arbitration awards. The Australian reasoning would suggest that engaged both the adjudicative immunity to register the awards and the enforcement immunity to arrest the shares. However, the Royal Court held that only the adjudicative immunity was engaged.

How come? The reason is that the Court considered the enforcement immunity is only engaged by enforcement of a judgment against the state in question.

Unsurprisingly, the Royal Court drew on Hemisphere. This ruled that separate entities' separate identities should be respected. So, where a state forms a separate company for commercial purposes, with its own management team and budget, the strong presumption was to respect that separation. It was not therefore the state, and it and the state could not mutually bear each other's liabilities.

In Tepe, it was not enforcement of a judgment (even after recognition of the awards) against the state and its property. It was enforcement of a judgment entered against a separate entity against that separate entity's property. It was not an attempt to enforce Turkey's obligation against Turkey's assets. It was an attempt to enforce Botas' obligations against its own, Botas', assets.

Under the second provisions of the Act above, enforcement immunity applies to the property of the state or may be engaged when a separate entity is acting as the state. A separate company is strongly presumed not to be the state, absent compelling evidence.

The first, adjudicative immunity provisions therefore applied and Botas was not able to avail itself of them.

The importance of the distinction

On one view, applying the adjudicative provisions of the Act could be seen to make things harder for Tepe or applicants to enforce, because they open the door to the state asserting immunity on the basis of an interest or control which may be less than a property interest as referred to in the enforcement provisions. So this could be seen as a lower standard for the state to achieve.

However, as the Australian court noted, enforcement immunity tends to be more absolute than immunity from adjudication. This reflects the different rationales for the two. Adjudicative immunity arises because sovereign states cannot be subjected to each other's adjudicative proceedings. However, enforcement immunity arises from reluctance to interfere with a sovereign's property.

The result is that, even when a party has obtained judgment against a state, it may still be unable to enforce that judgment against the assets of the state. That was the result in Firebird.

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In its application of the adjudicative provisions to enforcement against a separate company, the Jersey court confirmed that interest or control must have some legal basis, and indirect interest or control would not be enough. Otherwise, any indirect interest or control would extend immunity to any state owned company, and all that company's assets. That would overturn the provisions in the Act which expressly provide that entities separate from the state are not immune unless certain exceptions apply. If that were allowed, that would give not only states, but trading companies, a means of avoiding their liabilities.

Conclusion: good news

The Royal Court's decision is good news. Following the logic of Hemisphere brings a little more cohesion and certainty to a difficult area.

More importantly, however, the decision upholds a basic expectation that debts will be paid. Basically, if a company related to the state owes you money, it cannot simply rely on that relationship to avoid paying you – or you taking its assets if it does not.

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