SUPREME COURT OF VICTORIA

COURT OF APPEAL

No. 2035 of 2003

VICTORIA AIRCRAFT LEASING LIMITED & ORS	Appellants
v.	
UNITED STATES & ORS	Respondents

VICTORIA AIRCRAFT LEASING LIMITED & ORS	Appellants
v.	
WELLS FARGO BANK NORTHWEST, NATIONAL ASSOCIATION (in its capacity as security trustee for the Export-Import Bank of the United States) & ANOR	Respondents

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JUDGES:	CALLAWAY and BUCHANAN, JJ.A. and WILLIAMS, A.J.A.
WHERE HELD:	MELBOURNE
DATE OF HEARING:	16-17 February 2005
DATE OF JUDGMENT:	11 April 2005
MEDIUM NEUTRAL CITATION:	[2005] VSCA 76

Foreign state immunity – Transaction not a commercial transaction within the meaning of s.11 of the *Foreign States Immunities Act* 1985 (Cth).

Practice and procedure – Stay of proceedings – Presence of third party not necessary to resolve issues between plaintiff and defendants – Issues raised by defendants not justiciable as they concerned acts of foreign states – No sufficient connection between non-justiciable issues and plaintiff's claim to warrant stay.

APPEARANCES:	Counsel	Solicitors
For the Appellants	Dr C.L. Pannam, Q.C. Mr J. Manetta	Baker & McKenzie
For the United States	Dr G. Griffith, Q.C. Ms C.M. Harris	Kliger Partners
For the other Respondents	Mr R.A. Brett, Q.C. Ms P. Neskovcin	Allens Arthur Robinson

CALLAWAY, J.A.:

1 I have had the advantage of reading in draft the reasons for judgment prepared by Buchanan, J.A. I agree with his Honour, subject to one point that I should like to express in my own words. The relevant provisions of the *Foreign States Immunities Act* 1985 are set out in his judgment.

2 Section 11(3)(a), (b) and (c) of the Act describe three common classes of transaction. The first is a contract for the supply of goods or services, a concept familiar in legal practice and found in other Commonwealth legislation, like the *Trade Practices Act* 1974. I shall return to the second. The third is a guarantee or indemnity in respect of a financial obligation. The word "indemnity" takes its colour from "guarantee". The reference is to the familiar concept of a third party guaranteeing another person's financial obligation or accepting a primary liability in respect of it.

3 The second class of transaction described in s.11(3) is "an agreement for a loan or some other transaction for or in respect of the provision of finance". (If it were not for the words "or in respect of", that would refer to a loan or similar transaction in much the same way as one might refer to a sale or other supply of goods. The words "or in respect of" make it wider, but they should not be given such an expansive meaning as to render s.11(3)(c) otiose.) The critical question is whether the alleged agreement, as pleaded and particularized and assumed for present purposes, is a transaction *for or in respect of* the provision of finance. In my opinion, the agreement does not answer that description.

4 It was not submitted that the agreement could be broken up into its component parts so that, inter alia, there was a distinct agreement to do the things summarized in [9] below. There was a package of reciprocal obligations. For the reasons given by the learned trial judge and by Buchanan, J.A., it would be a mischaracterization of that package to say that it was a transaction for or in respect of the provision of finance. It had a much wider ambit, of which relief in relation to

the appellants' financial obligations was but one element.[1]

BUCHANAN, J.A.:

5 Wells Fargo Bank Northwest, National Association ("Wells Fargo"), a Utah company, brought proceedings in the Supreme Court to recover possession of a Boeing 737-400 aircraft from Nauru Aircraft Corporation ("NAC").

6 Wells Fargo acted as the security trustee for the mortgagee of the aircraft, the Export Import Bank of the United States ("Eximbank"), the second-named plaintiff in the action. Eximbank is an agency of the United States of America. The aircraft was purchased by Victoria Aircraft Leasing Limited ("VALL") with a loan guaranteed by Eximbank. VALL defaulted in the performance of its obligations as borrower and Eximbank's guarantee was called up. Eximbank paid out the loan and stood in the shoes of the lender.

7 The aircraft was operated by NAC, which carried on the business of an airline under the name "Air Nauru". The Republic of Nauru guaranteed to Eximbank the due performance of the obligations of VALL as borrower of the price of the aircraft. VALL and NAC are agencies of Nauru. VALL, NAC and the Republic of Nauru were the defendants to the proceeding. In its statement of claim Wells Fargo alleged that VALL failed to make repayments of the loan and committed other breaches which constituted events of default under the mortgage.

8 By their defence and counterclaim the defendants did not deny the debt owing to Eximbank or the mortgage, but pleaded that the obligations alleged by the plaintiffs were not enforceable by reason of an agreement made between Nauru and the United States of America by representatives of both countries. It was alleged that Nauru agreed to assist in the defection of a North Korean scientist to the United States, to co-operate with the United States to investigate the involvement of

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1 In my view it is not enough, as in the case of a grant of legislative power, to say that the alleged agreement is in respect of the provision of finance even if it is also in respect of other things. The question is whether it may fairly be described in the language of s.11(3)(b).

Nauruan organisations in the transfer of money for the purpose of international terrorism and to reform Nauru's laws to prevent money laundering and the production of false Nauruan passports.

9 It was alleged in paragraph 15 of the pleading that if Nauru co-operated with the United States agenda, the United States would:

> "(a) ensure that Eximbank would give Nauru additional time to pay its debts to Eximbank, sufficient to ensure the operational viability of Air Nauru;
>
> (b) provide funds to Nauru sufficient to eliminate any problems Nauru might have in relation to re-payment of the Eximbank financing; and
>
> (c) not permit Eximbank to exercise any strict contractual rights which it might have to take possession of and sell the aircraft."

10 In the particulars subjoined to this paragraph it was alleged that the agreement and representations were oral. The substance of the conversations constituting the agreement and representations was set out. From the particulars it is apparent that the defendants' case is that the United States promised to provide a broad range of assistance to Nauru as the price of Nauru's co-operation. The United States agreed to arrange to remove Nauru from a list of non-co-operative countries compiled by the Financial Action Task Force, an arm of the Organization for Economic Cooperation and Development ("OECD"). Nauru's inclusion on the list made it very difficult for Nauruan companies to do business with United States and OECD banks. The United States agreed to provide substantial assistance, monetary and otherwise, to enable Nauru to establish a modern international banking facility. The United States also agreed to undertake economic projects, such as a satellite research tracking station, to benefit the Nauruan economy. The United States' promise to assist Nauru in dealing with Eximbank was part of a larger promise to deal with Nauru's financial problems, not only with Eximbank, but also with Marriott Properties and GE Finance.

11 It was alleged that in consideration of the promises made by the United States and in reliance upon the United States' representations Nauru appointed representatives of the United States as diplomatic officials, took steps to reform its off-shore banking regime and introduced laws to control the misuse of Nauruan passports.

12 A third party notice was issued against the United States. The allegations in the statement of claim endorsed upon the notice mirrored those in the defence and counterclaim.

13 The third party entered a conditional appearance and applied to set aside the notice on the ground that the Court lacked jurisdiction to entertain the claim as the United States was entitled to immunity pursuant to the provisions of s.9 of the *Foreign States Immunities Act* 1985 (Cth) ("the Act"), which provides:

> "Except as provided by or under this Act, a foreign State is immune from the jurisdiction of the courts of Australia in a proceeding."

One exception is found in s.11, which provides:

> "(1) A foreign State is not immune in a proceeding in so far as the proceeding concerns a commercial transaction.
>
> (2) Subsection (1) does not apply:
>
> (a) if all the parties to the proceeding:
>
> (i) are foreign States or are the Commonwealth and one or more foreign States; or
>
> (ii) have otherwise agreed in writing; or
>
> (b) in so far as the proceeding concerns a payment in respect of a grant, a scholarship, a pension or a payment of a like kind.
>
> (3) In this section, 'commercial transaction' means a commercial, trading, business, professional or industrial or like transaction into which the foreign State has entered or a like activity in which the State has engaged and, without limiting the generality of the foregoing, includes:
>
> (a) a contract for the supply of goods or services;
>
> (b) an agreement for a loan or some other transaction for or in respect of the provision of finance; and
>
> (c) a guarantee or indemnity in respect of a financial obligation;
>
> but does not include a contract of employment or a bill of exchange."

"Proceeding" is defined as "a proceeding in a court …" (s.3(1)).

14 The United States did not concede the truth or accuracy of the case pleaded against it, but for the purposes of the application it was assumed that the allegations contained in the third party statement of claim were true. The application proceeded on the basis that the third party was entitled to immunity unless the arrangement between Nauru and the United States was a commercial transaction within the meaning of s.11. The United States also contended that if the arrangement was a commercial transaction, its immunity was restored by

s.11(2)(a)(i). It was submitted that the word "proceeding" in the sub-section was a drafting error: the clear intention of the legislature was to preserve immunity where all the parties to a transaction, rather than a proceeding, were foreign states.

15 The judge who heard the application held that the transactions specified in paragraphs (a), (b) and (c) in s.11(3) of the Act were qualified by the opening words of the sub-section. The specified transactions would be commercial transactions only if they had the necessary quality of a "commercial, trading, business, professional or industrial or like transaction". Accordingly, if a transaction was substantially, essentially or predominantly of a political, diplomatic, governmental or intelligence or like character, it was not a "commercial transaction" despite the fact that it incorporated some elements of the transactions specified in s.11(3)(a) to (c). Her Honour said:

> "Whether or not the transactions in s.11(3)(a)-(b) are ipso facto commercial, the incorporation of only subsidiary or minor 'commercial, trading, business, professional, industrial or like' elements in a transaction which is predominantly one of a political, diplomatic, governmental or intelligence character, or an admixture of those elements, in my view will not render it a 'commercial transaction'."

16 Her Honour found that the transaction between Nauru and the United States alleged in the third party statement of claim appeared "overwhelmingly non-commercial". Although the promises by the United States included the possible payment of funds which might be the provision of finance within the meaning of s.11(3)(b), the transaction viewed as a whole was of a diplomatic, governmental, intelligence and national security character.

17 The trial judge also held that s.11(2)(a)(i) should be read as if the word "transaction" replaced the word "proceeding" and thus immunity was conferred on the United States pursuant to the exception, for the only parties to the agreement alleged in the third party notice were Nauru and the United States.

18 Accordingly, her Honour set aside the third party notice on the basis that the Unites States was not amenable to the jurisdiction of Australian courts pursuant to the provisions of the Act.

19 The appellants contend that sovereign immunity was lost once the transaction fell

within one of the paragraphs (a), (b) and (c) in s.11(3) and the trial judge erred in also requiring the transaction to be of a type described in the opening words of the sub-section.

20 Relying upon the report of the Australian Law Reform Commission, which drafted the Act, the appellants contended that the legislature intended to wholly replace the common law with a new type of test. In 1975 the absolute doctrine of state immunity at common law[2] was replaced in England by an immunity restricted to claims where the act forming the basis of the claim was a "sovereign or public act" rather than an act of a private law character such as a private citizen might have entered into.[3] The distinction between sovereign and governmental transactions on the one hand and commercial and private transactions on the other hand was difficult to draw. The courts analysed the objective characteristics of transactions and the subjective purposes they were designed to achieve. The outcome generally depended on the particularity with which the evaluation was conducted, and the choice of the degree of particularity was arbitrary.

21 In the United Kingdom the *State Immunity Act* 1978 supplanted the common law. Subject to a residual provision preserving the test of restrictive immunity, transactions were classified according to their objective effects, for example, contracts for the supply of services, transactions for the provision of finance. Immunity was conferred or withheld for each type of transaction. If a foreign state entered into a specified transaction, it was a commercial transaction whether or not the foreign state exercised sovereign authority.

22 While I think there is some force in the contention that, despite its different structure, s.11 of the Act was intended to "adopt the substance of the United Kingdom provision"[4], it is not necessary to decide whether paragraphs (a), (b) and (c) are qualified by an additional requirement of commerciality. In my view the transaction entered into by Nauru and the United States did not meet any of the descriptions set out in the paragraphs.

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2 See *Compania Naviera Vascongado v. S.S. Cristina* [1938] A.C. 485; *The Porto Alexander* [1920] P.30.

3 *The Philippine Admiral* [1977] A.C. 373; *Trendtex Trading Corporation v. Central Bank of Nigeria* [1977] Q.B. 529.

4 A.L.R.C. Report [92].

23 In my opinion none of the paragraphs of sub-s.(3) applied to the promises made by the United States to Nauru. Paragraph (a) had no operation. Paragraph (b) contemplates a loan or like transaction. In my view it does not extend to a promise to influence the creditor to give his debtor extra time to pay or refrain from exercising rights under a security. Nor do I think that the paragraph extends to a promise to pay money which could be used by the recipient to repay a debt to another. Paragraph (c) is concerned with a guarantee of the performance of another's obligation. I think that the indemnity with which it is coupled connotes the assumption of a primary liability whether or not another makes default. The paragraph does not embrace a promise to prevent a creditor exercising rights under a security.

24 Even if an aspect of the transaction between Nauru and the United States literally fell within one or more of the paragraphs of sub-s.(3), nevertheless in my view the transaction viewed as a whole was not encompassed by the sub-section.

25 Each of the promises alleged to have been made by Nauru and each of the acts which it is alleged to have performed in reliance upon the representations said to have been made by the United States concerned governmental functions of Nauru. None of the promises or acts related to a contract for the supply of goods or services, an agreement for a loan or other transaction for or in respect of the provision of finance or a guarantee or indemnity in respect of a financial transaction. The actions to be undertaken by Nauru comprised activities relating to its diplomatic and foreign relations, national security, intelligence, terrorism and the reform of banking laws and passport abuse. The promises made by the United States did include an offer to assist Nauru to deal with its obligations to repay a loan and may have involved the provision of money to Nauru. The context in which that promise was made was that it was but one component in a number of measures answering the description of economic assistance to the government of Nauru.

26 In my opinion the vagueness of the terms alleged in paragraph 15 tells against the contention that the transaction amounted to an agreement in respect of the provision of finance or a guarantee or indemnity in respect of a financial obligation. The additional time to pay which the United States was alleged to have promised was no more specific than the time sufficient to ensure the operational viability of Air Nauru. Neither the amount of the

funds to be provided to Nauru nor the time when that provision was to be made was stated. The promises were somewhat inconsistent. Was the United States to pay the sums owing to Eximbank or was it to arrange time for Nauru to pay those sums? The obligations in commercial agreements are generally expressed in definite, quantifiable terms. The transaction between Nauru and the United States was expressed in terms more akin to political arrangements between states.

27 In my view the promises by the United States to deal with Nauru's difficulties in meeting its obligations to Eximbank were not the most significant or substantial element in the United States' offer of assistance. In the third party statement of claim those promises were alleged as the only consideration for the promises made by Nauru, and counsel for Nauru in his submissions described the promises as those regarded by Nauru as the most important component of the transaction. In my opinion the importance of the promise of assistance to meet Nauru's obligations to Eximbank is to be judged objectively, not from the narrow prism of Nauru's objectives in its negotiations with the United States or in the litigation.

28 I have taken into account the particulars as well as the substantive allegations in the third party statement of claim, for I think the transaction is to be evaluated by considering as a whole the conversations comprising it. The transaction cannot sensibly be segmented by isolating the promises made by the United States which might be said to answer the description of an agreement in respect to the provision of finance. Those promises were part of a package or program of assistance in return for political favours. In my opinion the transaction taken as a whole is not be accurately described as one for or in respect of the provision of finance or as a guarantee or indemnity in respect of a financial obligation.

29 For the foregoing reasons I am of the opinion that the trial judge correctly held that s.11 of the Act did not apply, and thus the immunity conferred by s.9 was not displaced. It is not necessary to determine whether the qualification to the exception in s.11(2)(a)(i) would have afforded immunity to the United States.

30 In the light of her Honour's decision the defendants applied to stay the proceedings by

Wells Fargo on two bases. The first was that the United States, a necessary party, was now absent. The second was that the principal issues raised in the defence were not justiciable as they required the determination of matters bearing upon the validity of the acts of foreign states and thus could embarrass the Court or prejudice the relationship of Australia with Nauru and the United States.

31 The defendants relied upon the representations made by the United States to Nauru to defeat Wells Fargo's claim. The defendants did not allege that Eximbank was bound by the acts of the United States as agent for Eximbank. Such a contention could not have been maintained in the light of the provisions of the *Export Import Bank Act* 1945, which established Eximbank. Eximbank's business consisted in supporting the export sales of goods manufactured in the United States by financing their purchase. All the issued shares in Eximbank were held by the President of the United States, who appointed its directors. All the profits of Eximbank were paid to the United States' treasury. Accordingly, the defendants pleaded that the failure by the United States to make good the representations rendered it unconscionable for the United States, through the agency of Eximbank, to take the benefit of the defendants' reliance on the representations, and thus Wells Fargo was precluded from exercising any rights over the aircraft under the mortgage.

32 The trial judge found that the issues raised in the defence and counterclaim were not justiciable. Her Honour said that the defence and counterclaim,

> "… would require the Court to consider and determine … uncertain and sensitive matters of espionage, intelligence, national security and diplomacy, and the elements and effect of an agreement and representations made in the course of high level dealings between representatives of two foreign sovereign nations. Such matters do not appear to be susceptible of resolution by reference to judicial standards available to an Australian court."

Nevertheless her Honour refused to stay the proceedings. She held that there was not a sufficiently clear connection between the claim of Wells Fargo and the non-justiciable issues to justify a stay.

33 As I have said, the promises by the United States relating to the obligations owed by Nauru to Eximbank were amorphous. The other aspects of the transaction appear even more vague and unformed. The United States would provide assistance to enable Nauru to

establish a modern international banking facility, to undertake economic projects to boost the economy of Nauru. Nauru was to assist the United States in the defection of a North Korean, to assist the United States in investigating the involvement of Nauru in organizations and their links with international terrorists and to reform Nauru's laws to prevent money-laundering and the production of false passports.

34 Whether Nauru and the United States had each carried out its side of the transaction involved questions which a municipal court of this country is not equipped to judge. Counsel for the appellants contended that the proceeding was concerned with ordinary principles of contract, estoppel and unconscionable conduct. Those may have been the causes of action invoked by the appellants, but their application to the subject matter of the negotiations between Nauru and the United States would take the Court into unchartered waters in that there are no judicial standards to judge questions such as whether Nauru adequately reformed its banking regime and appropriately co-operated with the United States in detecting and dealing with the activities of terrorists and whether the United States' plan to facilitate the defection of a North Korean scientist, possibly with the covert co-operation of China, was in fact implemented. The promises on both sides were not specifically enforceable, damages could not be assessed and equitable principles of municipal law did not enable the Court to determine whether the acts and omissions of States in their international relations were or were not unconscionable.[5]

35 In addition to the lack of what Lord Wilberforce in *Buttes Gas and Oil Co. v. Hammer (No. 3)*[6] called "judicial or manageable standards" by which to judge the issues, to embark upon an inquiry as to the content and performance of the promises which might be found to have emerged from negotiations between Nauru and the United States would involve the Court in a dispute of a kind that can only be resolved on a state to state level.[7]

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5 Counsel for the appellants referred to a proposed amended defence and counterclaim. No application to amend was made to the trial judge, and I think her Honour was entitled to determine the application for a stay on the basis of the existing pleading. In any event I do not consider that the appellants' case was advanced in any relevant respect by the proposed amendments.

6 [1982] A.C. 888 at 938.

7 *Kuwait Airways Corporation v. Iraqi Airways Company* [2002] 2 A.C. 883 at 971-2; *Petrotimor Companhia de Petroleos SARL v. Commonwealth of Australia* (2003) 126 F.C.R. 559.

36 Counsel for the appellants relied upon the decision of Cole, J. in *Australian Federation of Islamic Councils Inc. v. Westpac Banking Corporation*[8], in contending that it amounted to an abuse of the process of the Court for Eximbank to prosecute its claim while the appellants were unable to meet it by relying upon the transaction between Nauru and the United States.

37 The *Islamic Councils* case concerned funds deposited with the defendant by the ambassador of Saudi Arabia. The document evidencing the deposit stated that at maturity instructions would be given in writing by both an officer of the plaintiff and by the ambassador. The plaintiff subsequently instructed the defendant that its officers were to be the sole authorized signatories to the deposit, arguing that the fund belonged to it beneficially and the ambassador had surrendered all interest in and control of the funds. The defendant contended that the funds could not be dealt with save in accordance with the terms of the original agreement and argued that the ambassador was a necessary party in any suit concerned with deposit, and that as the ambassador and Saudi Arabia were immune from suit, the action should be stayed. Cole, J. held that the funds were the property of the Federation, but that the gift was subject to a condition that the control of the disposition of the funds was to be exercised by both the plaintiff and the ambassador. The ambassador had not waived his right to control the funds, and the defendant could only deal with the funds in accordance with the instructions of both parties. His Honour held that the ambassador was a necessary party to the proceedings because he was affected by the relief sought by the plaintiff. Accordingly the proceedings would be stayed.

38 In the *Islamic Councils* case the conduct of the ambassador and the country he represented lay at the heart of the plaintiff's case.[9] The contract relied upon by the plaintiff to establish its title to the funds was a tripartite contract between the plaintiff, the defendant and the ambassador, and the ambassador was directly affected by the relief sought by the plaintiff. In the present case the presence of the United States is not necessary in that sense to resolve the dispute between Eximbank and the defendants with respect to the defendants'

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8 (1998) 17 N.S.W.L.R. 623.

9 *Rahimtoola v. Nizam of Hyderabad* [1958] AC 379 is a like case.

obligations under the contract of loan and mortgage. The only effect which the proceedings may have upon the United States is that the outcome of the proceedings may affect the profits made by Eximbank, which are paid to the United States. The effect would be indirect and would be entirely the result of a gain or loss made or sustained by Eximbank. In the *Islamic Councils* case either the plaintiff or the ambassador was entitled to control the funds. In the present case the United States has no claim upon the aircraft the subject matter of the proceeding.

39 The defendants' application for a stay depended upon whether it would be unfair to determine Eximbank's claim when the defendants could make no claim over against the United States and could not rely upon the promises made by the United States as a defence to the claim by Eximbank. The question of fairness depends upon a weighing process involving the balancing of a variety of factors, including the detriment suffered by the appellants on the one hand and Eximbank on the other hand and the need to maintain public confidence in the administration of justice.[10]

40 Apart from the fact that Eximbank's claim does not involve any conduct by the United States, I consider that the question of fairness is affected by the difficulties faced by the appellants in fastening upon Eximbank responsibility for the acts of the United States. Eximbank played no part in the dealings between Nauru and the United States. It is not alleged in the defence and counterclaim that the United States was authorized by Eximbank to make any agreement or representations on its behalf. The provisions of the *Export Import Bank Act* referred to in paragraph [31] above establish that the United States is not the agent of Eximbank. The Act also makes it clear that Eximbank is not simply the alter ego of the United States.[11] The Act provides that Eximbank "shall constitute an independent agency of the United

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10 Cf. *Walton v. Gardiner* (1993) 177 C.L.R. 378 at 395-6 per Mason, C.J., Deane and Dawson, JJ.; *Rogers v. R.* (1994) 181 C.L.R. 251 at 256 per Mason, C.J. See also *State Bank of New South Wales v. Alexander Stenhouse Ltd.* (1997) Aust.Torts Reports 81-423 at 64,086.

11 Although the appellants contended that the Act was not observed and the United States government ran Eximbank as if it was a government department, in the absence of evidence to establish the contention, I think that for the purposes of the application for a stay the Act should be taken to accurately describe the relationship between Eximbank and the United States.

States …" (s.3(a)). Eximbank is under no general duty to obey the directions of the government or the President of the United States, save that the President can prevent Eximbank from dealing with certain countries.[12] It might be said to be unfair to visit upon Eximbank the alleged sins of the United States, for which it could be no more legally liable than a wholly owned subsidiary for the consequences of an agreement made by its holding company.

41 Further, the obligations alleged by the appellants arise out of a transaction between sovereign states concerning their political and international affairs and their relations with each other. It may be doubted whether Nauru or the United States intended their negotiations to result in a contract enforceable in any municipal court. In any event, disputes concerning such matters are properly dealt with by diplomacy rather than litigation in municipal courts. In my view fairness to Nauru does not require a stay of Eximbank's claim..

42 For the foregoing reasons I would dismiss the appeals.

WILLIAMS, A.J.A.:

43 I agree with Buchanan, J.A. that the appeals should be dismissed for the reasons he gives.

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[12] For example, Eximbank is not to extend credit in connection with the export of goods to Angola until the President certifies that free and fair elections have been held in Angola (s.2(b)(ii)).