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THE LIBYAN ASSET FREEZE AND ITS APPLICATION
TO FOREIGN GOVERNMENT DEPOSITS IN OVERSEAS
BRANCHES OF UNITED STATES BANKS: *LIBYAN
ARAB FOREIGN BANK v. BANKERS TRUST CO.*

Corinne R. Rutzke*

INTRODUCTION

United States asset freezes are political weapons invoked in response to international crises.¹ Traditionally, United States asset freezes have blocked foreign government assets within the jurisdiction of the United States.² Following the 1979 Iranian hostage crisis, however, United States peacetime asset freezes have attempted to block dollar-denominated accounts³ held in foreign branches⁴ of United States banks.⁵ An important legal issue associated with the use of peacetime blocking

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1. OFFICE OF FOREIGN ASSETS CONTROL, *BLOCKED FOREIGN ASSETS IN THE UNITED STATES* 1, 3 (1985) [hereinafter *TREASURY PAMPHLET*]. Historically, the blocking control orders, promulgated pursuant to section 5(b) of the Trading with the Enemy Act, authorized the President to regulate or prohibit any property transaction involving a foreign country or national during wartime. Trading with the Enemy Act of 1917, 50 U.S.C. app. § 5(b)(1)(B) (1982). Following the entry of the People's Republic of China into the Korean War in 1950, President Truman blocked Chinese and North Korean property within the jurisdiction of the United States. *The Management of Blocked Foreign Assets in the United States*, 12 INT'L CURRENCY REV. 37, 38 (No. 6 1980). Expanding the scope of the Trading with the Enemy Act, the International Emergency Economic Powers Act of 1977 permits the President, in peacetime, to nullify or prohibit any transfer or withdrawal of property where a foreign country or national has any interest. International Emergency Economic Powers Act of 1977, 50 U.S.C. § 1702 (a)(1)(B) (1982). Blocking controls, however, are not always employed as weapons against the assets of hostile governments. See Exec. Order No. 8,389, 3 C.F.R. § 644-45 (1940) (invoking the Trading with the Enemy Act to freeze the assets of the Norwegian and Danish governments). President Roosevelt invoked section 5(b) of the Trading with the Enemy Act to prevent the government of Nazi Germany from seizing the overseas assets of the vanquished Norwegian and Danish governments. *Id.*

2. Carswell & Davis, *Crafting the Financial Settlement*, in *AMERICAN HOSTAGES IN IRAN* 232-33 (P. Kreisberg ed. 1985) [hereinafter *Financial Settlement*].

3. See *infra* note 7 (explaining that foreign dollar-denominated accounts are routinely labeled as Eurodollar deposits).

4. See Lichtenstein, *U.S. Banks and the Eurocurrency Markets: The Regulatory Structure*, 99 BANKING L.J. 484, 493 n.25 (1982) (discussing the definition of "foreign branches").

5. See Carswell & Davis, *The Economic and Financial Pressures: Freeze and Sanctions*, in *AMERICAN HOSTAGES IN IRAN* 178 (P. Kreisberg ed. 1985) [hereinafter *Economic and Financial Pressures*] (describing the unprecedented blocking of Iranian government assets held in foreign branches of United States banks).

controls is whether the United States can use asset freezes to reach dollar-denominated accounts held in financial institutions outside the jurisdiction of the United States.⁶ Two recent cases involving peacetime asset freezes directed at Iranian and Libyan Eurodollar⁷ accounts examined this question.

President Carter, on November 14, 1979, declared a national emergency and froze all Iranian assets within or subject to United States jurisdiction, including all Iranian dollar-denominated accounts held in foreign branches of United States banks.⁸ Subsequently, the Iranian Central Bank, Bank Markazi Iran, sued the London branches of five United States banks⁹ and the Paris branches of two United States banks¹⁰ to recover the frozen Iranian Eurodollar accounts. The Algerian Accords between the United States and Iran, however, precluded the British and French courts from ruling on the legality of the extra-territorial application of a United States asset freeze.¹¹

6. Cutler, *Luncheon Address*, 1980 AM. SOC'Y INT'L L. PROC. 43, 45; see Financial Times, Oct. 18, 1986, at 4, col. 1 (remarking that no court has ever ruled on the extraterritorial effect of a United States asset freeze).

7. See Hoffman & Giddy, *Lessons from the Iranian Experience: National Currencies as International Money*, 3 J. COMP. CORP. L. & SEC. REG. 73, 76 (1981) (defining a Eurodollar account as a dollar-denominated bank deposit held in a bank outside the United States).

8. See Exec. Order No. 12,170, 3 C.F.R. § 457 (1980), reprinted in 50 U.S.C. § 1701 app. at 148 (1982) (ordering the blocking of all Iranian assets that come within the control of United States persons); Exec. Order No. 12,211, 45 Fed. Reg. 26,685 (1980), reprinted in 50 U.S.C. § 1701 app. at 149-50 (1982) (prohibiting the payment or transfer of funds to Iran); see also *Economic and Financial Pressures*, supra note 5, at 178-79 (noting that the Iranian asset freeze applied to Iranian Eurodollar accounts held in foreign branches of United States banks). President Carter ordered the Iranian asset freeze following the seizure of the United States embassy in Tehran. *Id.* at 175-77.

9. See Edwards, *Extraterritorial Application of the U.S. Iranian Assets Control Regulations*, 75 AM. J. INT'L L. 870, 876 (1981) (noting that Bank Markazi Iran sued the London branches of Bank of America National Trust and Savings Association, Bankers Trust Company, Chase Manhattan Bank N.A., Citibank N.A., and Manufacturer's Hanover Trust Co. to recover Iranian government deposits).

10. See *id.* at 876 (stating that Bank Markazi Iran sued the Paris branches of Citibank and Bank of America National Trust and Savings Association).

11. *Id.* at 870. The Algiers Accords provided for the release of American diplomatic and consular personnel from Iran. TREASURY PAMPHLET, supra note 1, at 29. The United States subsequently agreed to transfer all Iranian assets held in overseas branches of United States banks and in foreign branches of United States banks to the Algerian Central Bank in exchange for the release of the hostages. Declaration of the Government of the Democratic and Popular Republic of Algeria, Jan. 19, 1981, reprinted in 75 AM. J. INT'L L. 418, 418 (1981). The United States and Iran also agreed to establish an Iran-United States Claims Tribunal to adjudicate the claims of United States nationals against the United States. Declaration of the Government of the Democratic and Popular Republic of Algeria Concerning the Settlement of Claims by the Government of the United States of America and the Government of the Islamic Republic of Iran, Jan. 19, 1981, reprinted in 75 AM. J. INT'L L. 422, 422 (1981). See

On January 8, 1986, President Reagan, responding to Libyan threats against United States security and foreign policy interests,¹² froze all dollar-denominated assets of the Libyan government including assets held in foreign branches of United States banks.¹³ Following the announcement of the Libyan asset freeze, the Libyan Arab Foreign Bank (LAFB)¹⁴ requested the London branch of Bankers Trust Company to

Carter, *The Iran-United States Claims Tribunal: Observations on the First Year*, 29 UCLA L. REV. 1076, 1076-80, 1085-92 (1982) (discussing the creation of the new arbitral body and the reliance on the United Nations Commission on International Trade Law Rules (UNCITRAL) to provide the adjudicating framework of the Tribunal).

12. See Presidential Letter to the Speaker of the House and the President of the Senate Concerning the Libyan National Emergency, 22 WEEKLY COMP. PRES. DOC. 21 (Jan. 13, 1986) (stating that the President authorized sanctions under emergency decree in response to Libyan support of international terrorism); U.S. DEP'T OF STATE, SPECIAL REPORT NO. 138, LIBYA UNDER QUADHAFI: A PATTERN OF AGGRESSION 6 (1986) (noting the Libyan involvement in terrorism); N.Y. Times, Jan. 9, 1986, at A6, col. 1 (reporting the Reagan administration's assertion that Libya sponsored terrorist attacks at the Rome and Vienna airports on December 27, 1985, where five Americans died). The Libyan government, however, vehemently denied this accusation. Wash. Post, Aug. 31, 1986, at A25, col. 1.

13. Exec. Order No. 12,544, 3 C.F.R. § 183 (1987), reprinted in 50 U.S.C.A. § 1701 app. at 269 (West Supp. 1987). President Reagan issued Executive Order No. 12,544, declaring an emergency, pursuant to the International Emergency Economic Powers Act. *Id.* This act authorizes the declaration of an emergency if an event outside the United States constitutes an extraordinary threat to the national security, foreign policy, or economy of the United States. International Emergency Economic Powers Act, 50 U.S.C. § 1701(a) (1982). Prior to ordering the Libyan asset freeze, President Reagan prohibited United States citizens from trading with and traveling to Libya. Exec. Order No. 12,543, 3 C.F.R. § 181 (1987) reprinted in 50 U.S.C.A. § 1701 app. at 268 (West Supp. 1987). The precise rationale behind the asset freeze is unknown. Compare Wash. Post, Jan. 9, 1986, at A1, col. 5 (stating that the perceived Libyan withdrawal of dollar-denominated assets from United States banks, following the announcement of Libyan trade and travel sanctions on January 7, 1986, was a motivating factor behind the asset freeze) with Wall St. J., Jan. 9, 1986, at 6, col. 1 (proclaiming that the major reason for the freeze was to prevent Libya from collecting on American corporation bonds, guaranteeing performance of obligations arising under contracts with the Libyan government). The sanctions of January 7, 1986 rendered the performance of these contractual obligations impossible. *Id.*

14. See *Libyan Arab Foreign Bank v. Bankers Trust Co.*, [1986] L. No. 1567/L. No. 4048 (Q.B.) 1, reprinted in 26 I.L.M. 1600, 1603 (1987) (describing the Libyan Arab Foreign Bank as a Libyan corporation wholly owned by the Central Bank of Libya). The Libyan Arab Foreign Bank (LAFB) on May 13, 1986 commenced an action, L. No. 1567, in the High Court of Justice, Queen's Bench Division, Commercial Court, demanding repayment of \$131 million held in Bankers Trust Company's London account. *Libyan Arab Foreign Bank v. Bankers Trust Co.*, [1986] L. No. 1567 (Q.B.) 2. Justice Evans, of the High Court of Justice, found for the LAFB on its summary judgment motion and ruled that Bankers Trust Company must repay the funds. *Id.* at 3. Bankers Trust Company appealed this ruling to the Supreme Court of Judicature, Court of Appeal. *Id.* at 1, 2. The Court of Appeal, on December 19, 1986, reversed the ruling of Judge Evans, remanding the case back to the High Court of Justice. *Id.* at 21.

The LAFB, on December 23, 1986, sent a telex to Bankers Trust Company, de-

repay all funds held in the LAFB's London account.¹⁵ Bankers Trust Company refused to comply with this demand, claiming that the newly instituted asset freeze blocked the requested funds.¹⁶ Consequently, on May 13, 1986, the LAFB sued Bankers Trust Company to recover the balance of the account held in the London bank.¹⁷

Both the Iranian and Libyan situations expose the potential dilemma facing the foreign branches of United States banks subject to executive orders freezing dollar-denominated deposit accounts. Repayment of Eurodollar deposit accounts held in foreign branches of United States banks exposes the parent bank to criminal liability under United States law.¹⁸ If demands for repayment of frozen accounts are denied, however, United States banks face costly lawsuits and a potential loss of depositor confidence.¹⁹ This Case-Comment examines two arguments, the Eurodollar defense and the IMF defense, available to United States banks defending against claims for repayment of frozen Eurodollar accounts.

After providing a chronology of *Libyan Arab Foreign Bank v. Bankers Trust Co.*,²⁰ this Case-Comment analyzes Bankers Trust Company's assertion that an implied term of the banking relationship, derived from the operation of the Eurodollar market, excuses Bankers Trust Company from honoring the LAFB's demand for repayment.

manding payment again of \$131 million and \$161 million respectively. *Libyan Arab Foreign Bank v. Bankers Trust Co.*, [1986] L. No. 1567/L. No. 4048 (Q.B.) 17-18, *reprinted in* 26 I.L.M. 1600, 1611-12 (1987). When Bankers Trust Company did not honor the demand, the LAFB commenced a second action, L. No. 4048 in the High Court of Justice. *Id.* at 18. The High Court of Justice, on January 19, 1987, ordered L. No. 1567 and L. No. 4048 consolidated. *Id.* at 1, 18.

15. *Libyan Arab Foreign Bank v. Bankers Trust Co.*, [1986] L. No. 1567/L. No. 4048 (Q.B.) 17-18, *reprinted in* 26 I.L.M. 1600, 1611-12 (1987).

16. *Id.* at 17.

17. *Libyan Arab Foreign Bank v. Bankers Trust Co.*, [1986] L. No. 1567 (Q.B.) 2.

18. Exec. Order No. 12,544, 3 C.F.R. § 183 (1987), *reprinted in* 50 U.S.C.A. § 1701 app. at 269 (West Supp. 1987). The penalties for violating the provisions of the Libyan Sanctions Regulations are derived from section 206 of the International Emergency Economic Powers Act. International Emergency Economic Powers Act, 50 U.S.C. § 1705 (1982). *Id.* Section 206 states that violations of regulations promulgated under the Act are punishable by a civil penalty of not more than \$10,000. *Id.* Willful violation of regulations promulgated under the Act are punishable by fines of not more than \$50,000. *Id.* A natural person who willfully violates provisions of regulations issued pursuant to the Act is subject to imprisonment for no less than 10 years. *Id.* The Act will impose a similar penalty on an officer, director, or agent of a corporation that willfully violates regulations issued under the Act. *Id.*

19. *See supra* notes 9-10 and accompanying text (providing examples of the law suits that ensue following a bank's refusal to honor demands for repayment of Eurodollar deposits).

20. *Libyan Arab Foreign Bank v. Bankers Trust Co.*, [1986] L. No. 1567/L. No. 4048 (Q.B.) 1, *reprinted in* 26 I.L.M. 1600, 1603 (1987).

The implied term of the banking relationship, Bankers Trust Company contended, requires that repayment take place through processing systems in New York.²¹ Use of these systems, Bankers Trust Company argued, requires actions in New York that are illegal under United States law.²² Bankers Trust Company, therefore, claimed that the British doctrine of impossibility excused the bank from honoring the LAFB's demand for repayment.²³

This Case-Comment also examines a second possible defense available to foreign branches of United States banks holding frozen Eurodollar accounts. This argument, based on article VIII, section 2(b)²⁴ of the International Monetary Fund (IMF) Agreement, states that when the United States government freezes Eurodollar accounts, United States banks may claim that the accounts are actually exchange contracts involving United States currency.²⁵ Performance of the obligations arising under these exchange contracts, particularly the repayment obligations of the United States bank, would violate United States exchange control regulations promulgated in compliance with the IMF Agreement.²⁶ Consequently, under article VIII, section 2(b), neither Libya nor any other member of the IMF can seek to enforce these contracts.²⁷ In *Libyan Arab Foreign Bank v. Bankers Trust Co.*,²⁸ however, this IMF defense was inapplicable.²⁹ In future litigation this argument may provide a viable defense for foreign branches of United

21. *Id.* at 3.

22. *Id.*

23. *Id.* at 19.

24. Articles of Agreement of the International Monetary Fund, Dec. 27, 1945, 60 Stat. 1401, T.I.A.S. No. 1501, 2 U.N.T.S. 39 [hereinafter Agreement], reprinted in INTERNATIONAL MONETARY FUND, ARTICLES OF AGREEMENT 24 (1985).

25. See *Bank Markazi Iran v. Bank of America*, [1979] L. No. 5955 (Q.B.) 6, reprinted in IRANIAN ASSETS LITIGATION REPORTER 1028, 1033 (June 20, 1980) (raising the IMF defense in the context of the Iranian assets freeze litigation).

26. Edwards, *supra* note 9, at 881, 883.

27. See Decision No. 446-4, June 10, 1949, INTERNATIONAL MONETARY FUND, SELECTED DECISIONS OF THE INTERNATIONAL MONETARY FUND AND SELECTED DOCUMENTS 251 (11th issue 1985) [hereinafter SELECTED DECISIONS] (stating that if the requirements of article VIII, section 2(b) are fulfilled, judicial authorities of member countries should not assist other countries in circumventing valid exchange control restrictions, either through decreeing performance of contracts or awarding damages for their nonperformance); see also 2 A. DICEY & I. MORRIS, THE CONFLICT OF LAWS 1028 (10th ed. 1980) (noting that article VIII, section 2(b) transcends the general principles of conflict of laws). Therefore, if all the elements of article VIII, section 2(b) are met, British courts cannot enforce a Eurodollar deposit contract even if the place of performance is the United Kingdom, and British law governs the contract. SELECTED DECISIONS, *supra*, at 252.

28. *Libyan Arab Foreign Bank v. Bankers Trust Co.*, [1986] L. No. 1567 (Q.B.) 1.

29. *Id.* at 4-5 (noting that Bankers Trust Company did not raise the IMF defense in the context of the Libyan litigation).

States banks holding frozen Eurodollar accounts.

I. LIBYAN ARAB FOREIGN BANK V. BANKERS TRUST CO.

A. THE BANKING RELATIONSHIP

The LAFB opened a seven-day notice account³⁰ with the London branch of Bankers Trust Company in April 1973.³¹ Although a notice account, the investors used the London account primarily as a current account³² with interest paid on the balance.³³ In November 1977, Bankers Trust Company, dissatisfied with the operational difficulties and profit-generating capability of the LAFB's account, proposed the establishment of a managed account system, consisting of a current account with the New York office, and a call account with the London office.³⁴ The LAFB, however, rejected the managed account proposal.³⁵

Bankers Trust Company revived the managed account system proposal in 1980 and reached an agreement with the LAFB on December 11, 1980.³⁶ The managed account agreement established a demand account in New York with a peg or target balance of \$500,000 and a call account in London.³⁷ The agreement mandated that all LAFB transactions pass through the New York account.³⁸ At the beginning of each banking day, the agreement required the New York office of Bankers Trust Company to determine the closing balance of the New York ac-

30. See M. STIGUM, *THE MONEY MARKET MYTH, REALITY AND PRACTICE* 551 (1978) (characterizing call accounts as accounts that bear interest and require twenty-four hours notice prior to withdrawal).

31. *Libyan Arab Foreign Bank v. Bankers Trust Co.*, [1986] L. No. 1567/L. No. 4048 (Q.B.) 5, *reprinted in* 26 I.L.M. 1600, 1605 (1987).

32. *Id.* at 6.

33. *Id.* The terms of the deposit contract required the LAFB to give seven days notice prior to making withdrawals from the account. *Id.* at 5. Bankers Trust Company, however, never required the LAFB to adhere to this requirement. *Id.*

34. *Id.* at 6-7.

35. *Id.*

36. *Id.* at 7-9.

37. *Id.* at 9. A peg or target balance is a predetermined floor that mandates a minimum account balance. *Id.* at 7. The value of the peg balance reflects the amount necessary to compensate adequately Bankers Trust Company for its services. *Id.* The London account was denominated in Eurodollars. *Id.* at 9. A Eurodollar account is simply an account, located outside the United States, denominated in United States dollars. 9 L. WEERAMANTRY & W. SCHLICHTING, *BANKING LAW* § 211.05 (1986).

38. *Libyan Arab Foreign Bank v. Bankers Trust Co.*, [1986] L. No. 1567/L. No. 4048 (Q.B.) 8-9, *reprinted in* 26 I.L.M. 1600, 1607 (1987). Although the managed account arrangement did not contain explicit terms requiring the clearing of all transactions through the New York account, the court held that such a term was implied from the course of the negotiations establishing the arrangement. *Id.*

count for the previous day.³⁹ If the closing balance exceeded the peg or target balance, the agreement obligated the New York branch of Bankers Trust Company to transfer the excess amount to the London account.⁴⁰ Conversely, if the New York account balance fell below the peg balance, an appropriate transfer was made from the London account to the LAFB account in New York.⁴¹ Thus, the London account actually functioned as an interest bearing reservoir for the New York account.⁴² During the period of the LAFB's managed account system from December 1980 to December 1985, the relationship between Libya and the United States gradually deteriorated.⁴³

On December 27, 1985, terrorist attacks at the Rome and Vienna airports exacerbated already strained relations between Libya and the United States.⁴⁴ On the afternoon of January 7, 1986, Mr. Corrigan, the President of the Federal Reserve Bank of New York, contacted Mr. Brittain, the Chairman of Bankers Trust Company, to ascertain whether the Libyans removed funds from their bank accounts in the United States.⁴⁵ Mr. Brittain, after reviewing the account records, informed officials at the Federal Reserve Bank of New York that the Libyans had withdrawn funds from the United States.⁴⁶ Mr. Corrigan requested that Mr. Brittain temporarily halt all payments out of the Libyan accounts.⁴⁷ Following further discussions with Mr. Corrigan, Mr. Brittain contacted Treasury Secretary James A. Baker III to discuss the LAFB account.⁴⁸ Treasury Secretary Baker told Mr. Brittain

39. *Id.* at 7-9.

40. *Id.*

41. *Id.*

42. *Libyan Arab Foreign Bank v. Bankers Trust Co.*, [1986] L. No. 1567 (Q.B.) 8. Bankers Trust Company unilaterally altered the terms of the managed account arrangement in April 1984. *Libyan Arab Foreign Bank v. Bankers Trust Co.*, [1986] L. No. 1567/L. No. 4048 (Q.B.) 10, *reprinted in* 26 I.L.M. 1600, 1608 (1987). This modification effectively deprived the LAFB of one day's interest. *Id.* The complaint of LAFB included a breach of contract claim arising out of this modification. *Id.* at 3-5.

43. *Libyan Arab Foreign Bank v. Bankers Trust Co.*, [1986] L. No. 1567/L. No. 4048 (Q.B.) 9-10, *reprinted in* 26 I.L.M. 1600, 1607-08 (1987).

44. *See* N.Y. Times, Jan. 9, 1986, at A6, col. 1 (stating the Reagan administration position that the Libyan government was responsible for the attacks at the Rome and Vienna airports).

45. *Libyan Arab Foreign Bank v. Bankers Trust Co.*, [1986] L. No. 1567/L. No. 4048 (Q.B.) 13, *reprinted in* 26 I.L.M. 1600, 1609 (1987).

46. *Id.*

47. *Id.*

48. *Id.* at 14. When Bankers Trust Company learned that the LAFB made deposits into its New York accounts, Mr. Brittain contacted the Federal Reserve Bank in New York and informed officials that Bankers Trust Company would resume honoring the payment instructions of the LAFB. *Id.* Mr. Corrigan advised Mr. Brittain to contact Treasury Secretary Baker before making payments out of the Libyan accounts. *Id.*

that President Reagan had recently signed Executive Order No. 12,544,⁴⁹ rendering it illegal for Bankers Trust Company or any other American bank to make any payments out of Libyan accounts.⁵⁰

The LAFB, on April 28, 1986, sent two telexes to Bankers Trust Company's London branch.⁵¹ The first telex demanded repayment of the \$131 million balance in the London account, and the second telex demanded repayment of the \$161 million into the London account on January 8, 1986 based on Bankers Trust Company's obligation to transfer excess funds pursuant to the managed account agreement.⁵² Bankers Trust Company refused to honor either demand, arguing that Executive Order No. 12,544 blocked the transfers.⁵³ The LAFB, on December 23, 1986, made a final demand for repayment of the London account balance.⁵⁴ Once again, Bankers Trust Company refused the demand for repayment, claiming that honoring the demand would violate United States law.⁵⁵ Following this refusal, the LAFB initiated suit against Bankers Trust Company in the United Kingdom.⁵⁶

49. See Exec. Order No. 12,544, 3 C.F.R. § 183 (1987), *reprinted in* 50 U.S.C.A. § 1701 app. at 269 (West Supp. 1987) (freezing Libyan assets within the control of United States citizens).

50. *Libyan Arab Foreign Bank v. Bankers Trust Co.*, [1986] L. No. 1567/L. No. 4048 (Q.B.) 14, *reprinted in* 26 I.L.M. 1600, 1610 (1987). At the time of the freeze, the balance of the London account totalled approximately \$131 million. *Id.* at 4, 17. The balance of the New York account at 2:00 p.m. on January 8, 1986, after subtracting the peg balance, totalled approximately \$161.4 million. *Id.* at 12. According to the terms of the modified managed account arrangement, the bank should have transferred this sum to the London account at 2:00 p.m. on January 8, 1986. *Id.* at 17. The court concluded that if Bankers Trust Company had complied with the terms of the modified managed account arrangement, the balance of the London account at the time of the freeze would have totalled approximately \$292 million. *Id.* at 58.

51. *Id.* at 17.

52. *Id.*; see 1 W. SCHLICHTING, J. RICE & J. COOPER, *BANKING LAW*, § 9.05 (1987) [hereinafter *BANKING LAW*] (noting that a demand for repayment is essential to enforcing an obligation of the depositing bank).

53. *Libyan Arab Foreign Bank v. Bankers Trust Co.*, [1986] L. No. 1567/L. No. 4048 (Q.B.) 17, *reprinted in* 26 I.L.M. 1600, 1611 (1987). Bankers Trust Company claimed that honoring the demands for repayment would violate the executive order and the regulations promulgated pursuant to it. *Id.*

54. *Id.* at 17-18. The LAFB demanded payment in United States dollars or in sterling. *Id.*

55. *Id.* at 17.

56. See *id.* at 4-5 (listing the LAFB's six claims against Bankers Trust Company). The two principal claims involved the precise balance of the London account on January 8, 1986 and whether the LAFB was entitled to demand repayment of the London account balance. *Id.* at 4. This Case-Comment focuses exclusively on the latter claim and Bankers Trust Company's defenses to the LAFB's demands for repayment of the London account balance.

B. THE ISSUES OF THE SUIT

1. The Conflict of Laws Threshold

In *Libyan Arab Foreign Bank v. Bankers Trust Co.*,⁵⁷ the court began its examination of the case with a review of the rules governing the conflict of laws.⁵⁸ Under English law, Bankers Trust Company is excused from its contractual obligations to honor the LAFB's demands for repayment of the dollar-denominated London account, if repayment is illegal under the proper substantive law governing the managed account system.⁵⁹ Additionally, if repayment is not illegal under the proper substantive law of the contract, Bankers Trust Company is still excused from honoring the LAFB's demand for repayment of the London account balance when repayment "necessarily" requires performance of an act in a place where performance of that act is illegal.⁶⁰

Bankers Trust Company asserted that New York law was the proper substantive law governing the managed account arrangement.⁶¹ Bankers Trust Company contended that because New York law renders any payments out of the accounts illegal, a bank was excused from honoring the LAFB's demands for repayment of the London account balance.⁶² Thus, the British court was faced with the threshold question of whether the laws of New York or the laws of the United Kingdom were the proper substantive laws governing the managed account arrangement.

In a conflict of laws scenario, a court usually applies the law of the forum to determine how to properly characterize the case.⁶³ Under the laws of the United Kingdom, deposit arrangements are characterized as contracts.⁶⁴ Determining the proper substantive law governing a contract requires a court to apply the entire body of the forum's conflict of laws rules.⁶⁵ In the absence of a contractual choice of law clause, British courts look to the circumstances surrounding the establishment of the deposit contract to infer the intentions of the parties as to the appli-

57. *Libyan Arab Foreign Bank v. Bankers Trust Co.*, [1986] L. No. 1567/L. No. 4048 (Q.B.), reprinted in 26 I.L.M. 1600 (1987).

58. *Id.* at 3.

59. *Id.* at 19.

60. *Id.*

61. *Id.* at 3.

62. *Id.*

63. See A. DICEY & I. MORRIS, supra note 27, at 474-84 (stating that a court, in determining the nature of the case before it, will usually look to the law of the forum).

64. F. PERRY, LAW AND PRACTICE RELATING TO BANKING 53 (3d ed. 1981); T. REEDAY, THE LAW RELATING TO BANKING 1 (3d ed. 1976).

65. R. GOODE, COMMERCIAL LAW 913-14 (1982).

cable substantive law.⁶⁶ As with most Eurodollar deposit arrangements, the agreement between the LAFB and Bankers Trust Company did not contain a choice of law clause, nor were the intentions of the parties ascertainable from objective factors.⁶⁷ In these types of situations, the critical factor determining the proper law governing the contract is the doctrine of *lex situs*, the law of the place where the deposit is kept.⁶⁸

Applying the doctrine of *lex situs*, the court concluded that the managed account arrangement had two distinct components: the New York demand account and the London call account.⁶⁹ The court found that although the laws of New York were the proper substantive laws governing the New York account,⁷⁰ the laws of the United Kingdom were the proper substantive laws governing the London account.⁷¹ Therefore, because the executive order freezing the LAFB's accounts was not incorporated into English law,⁷² the court concluded that repayment of the London account balance was not illegal under the proper substantive law governing the contract. Bankers Trust Company, therefore, was not excused from honoring the LAFB's demands for repayment of the London account balance.⁷³

2. *The Eurodollar Defense*

In addition to the conflict of laws issue, the English court also evaluated the Eurodollar defense Bankers Trust Company presented. The crux of the Eurodollar defense is that the repayment of the LAFB's Eurodollar account in London cannot occur without the use of the pay-

66. I. CHITTY, *CONTRACTS* 1168-70 (25th ed. 1983).

67. See Carreau, *The Legal Aspects of International Deposit Contracts*, in *INTERNATIONAL CONTRACTS* 157-60 (Smith ed. 1981) (stating that ordinarily Eurodollar deposit contracts contain neither choice of law clauses nor provide an objective basis for ascertaining the intentions of the parties); see also *Libyan Arab Foreign Bank v. Bankers Trust Co.*, [1986] L. No. 1567/L. No. 4048 (Q.B.) 23, reprinted in 26 I.L.M. 1600, 1614 (1987) (implying that the two parties disagreed as to whether they intended New York law or United Kingdom law to govern the contract).

68. *Legal Repurcussions of the Freezing of Iranian Assets and Loans*, 12 INT'L CURRENCY REV. 25, 35 (No. 1 1980) [hereinafter *Legal Repurcussions*]; A. DICEY & I. MORRIS, *supra* note 27, at 1290-92.

69. *Libyan Arab Foreign Bank v. Bankers Trust Co.*, [1986] L. No. 1567/L. No. 4048 (Q.B.) 25, reprinted in 26 I.L.M. 1600, 1612 (1987).

70. *Id.* at 26.

71. *Id.*

72. *Legal Repurcussions*, *supra* note 68, at 35.

73. *Libyan Arab Foreign Bank v. Bankers Trust Co.*, [1986] L. No. 1567/L. No. 4048 (Q.B.) 19, reprinted in 26 I.L.M. 1600, 1612 (1987) (stating that the performance of a contract is excused when it has become illegal under the proper law of the contract). Because the performance is not illegal under United Kingdom law, Bankers Trust Company's performance of the contract is not an excuse. *Id.* at 26.

ment processing systems in the United States. This method, however, is illegal under United States law because of the asset freeze. It is a well established principle of British law that a party to a contract governed under English law is excused from performance of the contract when performance "necessarily involves doing an act which is unlawful by the law of the place where the act has to be done."⁷⁴ Bankers Trust Company, in its Eurodollar defense, asserted that the terms of the managed account arrangement specifically required all transactions involving the LAFB's accounts to pass through its New York office.⁷⁵ Alternatively, Bankers Trust Company contended that the established practice of the international Eurodollar market limited the methods of repayment the LAFB was entitled to demand.⁷⁶ Bankers Trust Company argued that complying with the LAFB's demand for repayment of its London Eurodollar deposits necessitated use of either the Clearing House Interbank Payments System (CHIPS)⁷⁷ or Fedwire⁷⁸ mecha-

74. *Id.* at 19. The House of Lords in *Regazzoni v. K.C. Sethia, Ltd.* examined whether performance of a sales contract necessarily involved any illegal action in a foreign country. *Regazzoni v. K.C. Sethia, Ltd.*, [1957] 3 All E.R. 286. In this case, *Regazzoni*, a Swiss resident, agreed to purchase 500,000 jute bags c.i.f. Genoa from *K.C. Sethia*, an English company. *Id.* at 288. *Regazzoni* informed the English company of his intention to reexport the jute bags to South Africa. *Id.* at 293. When the parties entered the agreement, they knew that they could only obtain the bags from India, which prohibited the export of any goods destined for South Africa. *Id.* at 288. The House of Lords found that as the underlying performance of the sales contract violated Indian law, its performance necessarily involved illegal action under foreign law. *Id.* at 288, 292-94. Thus, enforcement of the contract was against English public policy. *Id.*; cf. *Libyan Arab Foreign Bank v. Bankers Trust Co.*, [1986] L. No. 1567/ L. No. 4048 (Q.B.) 22, *reprinted in* 26 I.L.M. 1600, 1614 (1987) (noting that the Libyan bank did not intend to perform any illegal acts in New York).

75. *Libyan Arab Foreign Bank v. Bankers Trust Co.*, [1986] L. No. 4048 (Q.B.) 9, *reprinted in* 26 I.L.M. 1600, 1607 (1987). The court, however, found that the LAFB was entitled to unilaterally alter or terminate the managed account arrangement on 24 hours notice. *Id.* at 38. The court concluded that the LAFB had, in fact, terminated the managed account arrangement either implicitly through the telex of April 28, 1986 or expressly through their solicitor on July 30, 1986. *Id.* at 39. Therefore, on December 23, 1986, the time of the final demand for repayment, the managed account arrangement was not in effect, and the LAFB was not contractually required to conduct its transaction through Bankers Trust Company New York office. *Id.*

76. *Id.* at 40.

77. See *infra* notes 121-23 and accompanying text (describing the CHIPS dollar clearing system used to provide repayment of a Eurodollar deposit).

78. See BANKING LAW, *supra* note 52, § 8.02[7] (describing the Federal Reserve's use of Fedwire as a method of an electronic funds transfer). The Fedwire system allows electronic settlement between member banks. *Id.*; see also *id.*, § 82.02[1] - 82.02[5] (discussing the ways the Federal Reserve operates the Fedwire system). Most Eurodollar transfers, however, take place through the CHIPS system and not Fedwire because foreign banks, with the exception of central banks, are not members of the Federal Reserve System and have no access to Fedwire. Carreau, *supra* note 67, at 162. A United States member bank may opt to use Fedwire. *Id.* The CHIPS system, however, is more frequently used. See N. PENNY & D. BAKER, THE LAW OF ELECTRONIC FUND

nisms located in the United States.⁷⁹ Because using either system would necessarily involve conduct in the United States that was illegal in light of Executive Order No. 12,544, Bankers Trust Company argued that it was excused from its contractual obligation to honor the LAFB's demands for repayment of the London account balance.⁸⁰ Bankers Trust Company's reliance on a defense implied from the practice of the international Eurodollar market required the court to undertake an investigation into the operation of the international Eurodollar market.

3. *The History of the Eurodollar*

Several factors have contributed to the development of the Eurodollar market. The Soviet Union decided to begin holding dollar deposits outside of the United States in 1957.⁸¹ Some commentators considered this action the origin of the Eurodollar market.⁸² The Soviet Union deposited funds outside the jurisdictional reach of the United States to limit the ability of the United States to freeze Soviet assets.⁸³ Thus, investors held their funds in politically secure dollar-denominated accounts in London.⁸⁴ Other countries soon followed the Soviet

TRANSFER SYSTEMS § 9.04 (1980) [hereinafter ELECTRONIC TRANSFER SYSTEMS] (noting that CHIPS handles more than 90% of interbank transfers of United States dollars on any given day).

79. See *infra* notes 101-49 and accompanying text (discussing the operations of the Eurodollar markets and the potential effects of those operations on the LAFB's demands for repayment of their London Eurodollar deposits).

80. *Libyan Arab Foreign Bank v. Bankers Trust Co.*, [1986] L. No. 1567/L. No. 4048 (Q.B.) 40-42, *reprinted in* 26 I.L.M. 1600, 1623-24 (1987).

81. S. KHOURY, DYNAMICS OF INTERNATIONAL BANKING 24 (1980).

82. *Id.*; Korth, *International Financial Markets* in THE INTERNATIONAL BANKING HANDBOOK 11 (W. Baughn & D. Mandich ed. 1983). *Contra* R. JOHNSTON, THE ECONOMICS OF THE EURO-MARKET 10 (1982) (questioning the view that overseas deposits of the Soviet Union were the leading impetus behind the growth of the billion dollar Eurodollar market). Another factor contributing to the creation of the Eurodollar market in the 1950s involved the British prohibition on the use of sterling for financing international trade transactions between nonsterling area countries. R. MCKINNON, MONEY IN INTERNATIONAL EXCHANGE 201-02 (1979). Consequently, the dollar replaced the British pound as the vehicle currency of international trade, leading to a dramatic increase in financing arrangements denominated in dollars. R. JOHNSTON, *supra*, at 10. The International Monetary Fund prompted the growth of the Eurodollar market in establishing the dollar as the vehicle currency for financing third-party trade and as a reserve currency in 1945. S. KHOURY, *supra* note 81, at 25.

83. P. OPPENHEIM, INTERNATIONAL BANKING 294 (1983). The Soviet Union transferred its funds from the United States to the Moscow Narodny Bank in London and the Banque Commerciale pour L'Europe du Nord in Paris. D. KANE, THE EURODOLLAR MARKET AND THE YEARS OF CRISIS I (1983).

84. N. DEAK & J. CELUSAK, INTERNATIONAL BANKING 167 (1984). Eurodollars are generally free from any government controls. Korth, *supra* note 82, at 9; S. KIM & S. MILLER, COMPETITIVE STRUCTURE OF THE INTERNATIONAL BANKING INDUSTRY 18-

example.⁸⁵

A second factor stimulating the development of the Eurodollar market involved the effects of Regulation Q⁸⁶ on United States and foreign investors. Regulation Q placed restrictions on the amount of interest United States banks could pay on domestic deposits.⁸⁷ United States investors, seeking a high profit yield on their money, opened Eurodollar accounts during the tight money years of 1968 and 1969.⁸⁸ Regulation Q only applied to banks located in the United States, and European banks could, therefore, offer higher interest rates for deposits and attract dollar deposits at the expense of United States banks.⁸⁹ Thus, investors placed an increased amount of their dollars into Eurodollar accounts.

A third factor facilitating the growth of the Eurodollar market involved United States programs in the 1960s designed to reduce the American balance of payments deficit.⁹⁰ In 1963, President Kennedy sponsored the Interest Equalization Tax Act.⁹¹ This Act taxed the yield on foreign securities, discouraging United States citizens from purchasing foreign investments.⁹² In 1965, the United States government im-

19 (1983).

85. See D. KANE, *supra* note 83, at 2 (referring to the expansion of Eurodollar accounts in the London financial market in the late 1950s following the Soviet deposits of funds into that market); M. STIGUM, *supra* note 30, at 105 (noting that other Communist countries in addition to the Soviet Union began to place funds in the Eurodollar market in the late 1950s).

86. 12 C.F.R. § 217 (1982).

87. *Id.*; Effros, *The Whys and Wherefores of Eurodollars*, 23 BUS. LAW. 629, 637-38 (1968) (discussing the limitations that Regulation Q places on payment of interest on sight deposits and time deposits); D. KANE, *supra* note 83, at 2 (noting that Regulation Q also restricts the payment of interest on demand deposits).

88. M. STIGUM, *supra* note 30, at 106; see R. JOHNSTON, *supra* note 82, at 14-15 (noting that Regulation Q restricted the yields on deposits placed with United States banks).

89. D. KANE, *supra* note 83, at 2.

90. M. STIGUM, *supra* note 30, at 106. Several monetary scholars assert that the consistent United States balance of payments deficits were an important stimulus behind the development of the Eurodollar market. G. YOSSY, *INTERNATIONAL MONEY FLOWS AND CURRENCY CRISIS* 75-76 (1984); S. KHOURY, *supra* note 81, at 26; D. KANE, *supra* note 83, at 142. The central contention of these monetary analysts is that as the United States spent more money abroad than it earned, the deficit funneled dollars from the United States to Europe. G. YOSSY, *supra*, at 75. European banks, able to offer higher interest rates than United States banks, became a natural receptacle for the large dollar balances accumulated overseas. P. EINZIG & B. QUINN, *THE EURODOLLAR SYSTEM* 19 (1977). *Contra* A. CROCKETT, *INTERNATIONAL MONEY* 179 (1979) (refuting the assessment that the United States balance of payments deficit facilitated the rapid expansion of the Eurodollar market).

91. Interest Equalization Tax Act of 1963, Pub. L. No. 88-563, 78 Stat. 809 (1964) (retroactive to July 19, 1963) (repealed 1974).

92. S. KHOURY, *supra* note 81, at 25; R. MCKINNON, *supra* note 82, at 203. A consequence of the Interest Equalization Tax Act was the increased demand for me-

posed the Voluntary Foreign Credit Restraint Program on United States commercial banks.⁹³ This Program prohibited United States banks and other financial institutions from making loans to foreigners on a short-term basis.⁹⁴ The foreign direct investment regulations replaced the Voluntary Foreign Credit Restraint Program in 1968.⁹⁵ The foreign direct investment regulations permitted United States multinational corporations involved in direct investment to finance a foreign investment outside the United States.⁹⁶ Therefore, United States banks, opening overseas branches to service their multinational clients, spurred the growth of the Eurodollar market.⁹⁷

A final stimulus behind the development of the Eurodollar market involved an increase in the surplus reserves of the Organization of Petroleum Exporting Countries (OPEC).⁹⁸ When oil prices rose in the 1970s, OPEC members funneled their excess cash reserves into the Eurocurrency market.⁹⁹ The OPEC members, therefore, placed a large surplus of dollars in Eurodollar accounts.¹⁰⁰

4. *The Nature of Eurodollars*

The LAFB, in its original motion for summary judgment, asserted that the London account was not a Eurodollar account and that it was therefore inappropriate to imply a term from the practices of the international Eurodollar market.¹⁰¹ Bankers Trust Company, however,

dium- and long-term finance in the Eurodollar capital markets. R. JOHNSTON, *supra* note 82, at 13-14; G. YOSSY, *supra* note 90, at 77-78.

93. M. STIGUM, *supra* note 30, at 107.

94. R. MCKINNON, *supra* note 82, at 203; M. STIGUM, *supra* note 30, at 107.

95. 15 C.F.R. §§ 1000-1050 (1974), issued pursuant to Exec. Order No. 11,387, 33 Fed. Reg. 47 (1968), revoked 40 Fed. Reg. 30,481 (1974).

96. S. KHOURY, *supra* note 81, at 25.

97. S. KIM & S. MILLER, *supra* note 84, at 20. The foreign branches of United States banks also realized their potential to service foreign companies in the local banking market seeking financial and corporate business information for purposes of transacting business in the United States. *Id.*

98. N. DEAK & J. CELUSAK, *supra* note 84, at 167-68.

99. M. STIGUM, *supra* note 30, at 107; N. DEAK & J. CELUSAK, *supra* note 84, at 167-68. At one point, the OPEC nations were the largest single source of funds for the entire Eurocurrency market. *Id.*

100. N. DEAK & J. CELUSAK, *supra* note 84, at 168; see Crane & Hayes, *The International Role of U.S. Banks in Perspective*, in INTERNATIONAL BANKING 463 (E. Roussakis ed. 1983) (stating that at the end of 1980, oil exporting countries held approximately \$335 billion in Eurodollar accounts). Of this sum, approximately \$105 billion belonged to six oil exporting countries: Libya, Iraq, Iran, Oman, Trinidad and Tobago, and Brunei. *Id.* at 465.

101. Financial Times, Dec. 4, 1986, at 6, col. 3; see F. MANN, THE LEGAL ASPECTS OF MONEY 195 (4th ed. 1982) (remarking that a depositor can hold a dollar-denominated account outside the United States that is not characterized as a Eurodollar ac-

noted that a call account payable on demand, involving multiples of \$1 million, was a contract within the scope of the Eurodollar market.¹⁰² Thus, the English court had to determine whether the London account was a Eurodollar account.¹⁰³ Answering this question required an examination of the nature of Eurodollar accounts, the manner in which the LAFB used the London account, and the methods Bankers Trust Company used to manage the account.

Determining the exact nature of a Eurodollar account requires a review of the definition of a Eurodollar and its characteristics. The commonly accepted definition of a Eurodollar is a dollar-denominated bank deposit located outside the United States.¹⁰⁴ Most commentators assert that Eurodollars are usually held in nonnegotiable, fixed-term time deposits¹⁰⁵ or in negotiable, Eurodollar certificates of deposit.¹⁰⁶ Scholars analyzing the nature of Eurodollar accounts argue, however, that call accounts payable on demand are also properly included within the scope of the Eurodollar market.¹⁰⁷ Justice Evans, granting a summary

count). Distinguishing between an ordinary dollar-denominated deposit and a Eurodollar deposit requires consideration of how the depositor uses the account and how the bank manages the account. *Id.*

102. *Libyan Arab Foreign Bank v. Bankers Trust Co.*, [1986] L. No. 1567 (C.A.) 14.

103. *See id.* at 9 (noting that in the lower court, Justice Evans held in his summary judgment motion that the London account was not a Eurodollar account). Justice Evans relied on the affidavits of two monetary experts to characterize the London account. *Id.* at 14-15. These affidavits argued that the exceedingly long maturity of the London account and the Bankers Trust Company practice of providing account statements to the LAFB indicated that the London account was an ordinary dollar deposit account rather than a Eurodollar account. *Id.* at 15-17. Accordingly, Justice Evans of the High Court of Justice, granted the LAFB's motion for summary judgment. On appeal, however, Justice Kerr of the Court of Appeal, noting that such considerations were inappropriate in the context of a summary judgment motion, reversed Justice Evans's ruling. *Id.* at 17.

104. L. WEERAMANTRY & W. SCHLICHTING, *supra* note 37, § 211.05; Korth, *The Eurocurrency Markets*, in *THE INTERNATIONAL BANKING HANDBOOK* 17 (W. Baughn & D. Mandich eds. 1983) [hereinafter *Eurocurrency Markets*].

105. *See* L. WEERAMANTRY & W. SCHLICHTING, *supra* note 37, § 9.07 (explaining that a time deposit is a deposit for a certain period of time, where the depositor generally does not have a right to withdraw a deposit for a period of 14 days or more after the date of the deposit).

106. *See* Roussakis, *Glossary of Financial Terms* in *INTERNATIONAL BANKING* 517 (E. Roussakis ed. 1983) (defining the negotiable certificate of deposit as a large denomination certificate of deposit that can be sold but cannot be cashed in before maturity). From the point of view of investors, Eurodollar time deposits having fixed maturities also have the disadvantage of illiquidity. M. STIGUM, *supra* note 30, at 115. Citibank, however, was the first bank to provide liquidity to Eurodollar certificates by issuing Eurodollar certificates of deposit in London. *Id.* Other United States banks and foreign banks with London branches soon followed Citibank's lead. *Id.*

107. M. STIGUM, *supra* note 30, at 113; F. LEES, *INTERNATIONAL BANKING AND FINANCE* 293 (1974); *see* *Libyan Arab Foreign Bank v. Bankers Trust Co.* [1986] L.

judgment for LAFB effectively rejected attempts to expand the scope of the Eurodollar market to include call accounts payable on demand.¹⁰⁸ At a full trial, Justice Staughton ruled instead that a call account fell within the scope of the Eurodollar market.¹⁰⁹

A further consideration of the additional characteristics of Eurodollar accounts is necessary to determine whether it is possible to properly classify the LAFB's London account as a Eurodollar account. Eurodollar accounts typically have three common attributes. First, Eurodollar deposits are generally interest-bearing accounts in an amount exceeding \$1 million.¹¹⁰ Second, unlike an ordinary dollar deposit, a depositor does not make payments into or withdrawals from a Eurodollar account through the use of a check.¹¹¹ Third, most scholars agree that commercial banks are often the owners of Eurodollar deposits.¹¹²

Examining the available facts, the British court, at a full trial, concluded that the London account was a Eurodollar account.¹¹³ First, the LAFB maintained the London account balance at approximately \$200 million.¹¹⁴ Second, the account was an interest-bearing account during all relevant times pertaining to the Libyan litigation.¹¹⁵ Third, the

No. 1567 (C.A.) 16 (examining the affidavits of two monetary analysts who included call accounts within the scope of the Eurodollar market). *Contra Eurocurrency Markets*, *supra* note 104, at 16; P. OPPENHEIM, *supra* note 83, at 297 (stating that only time deposits are considered as Eurodollar deposits). One commentator has suggested that many banks retain call accounts because call money is cheap, the investor can withdraw on one day's notice, and it is a stable source of funds. M. STIGUM, *supra* note 30, at 113.

108. See *Libyan Arab Foreign Bank v. Bankers Trust Co.* [1986] L. No. 1567 (C.A.) 7, 9 (stating that the London account was at all relevant times a call account, payable on demand and, thus, not properly within the scope of the Eurodollar market).

109. *Libyan Arab Foreign Bank v. Bankers Trust Co.*, [1986] L. No. 1567/ L. No. 4048 (Q.B.) 1, *reprinted in* 26 I.L.M. 1600, 1603-04 (1987).

110. A. CROCKETT, *supra* note 90, at 169 (maintaining that the usual Eurodollar deposit is \$1 million); J. LITTLE, EURODOLLARS-THE MONEY-MARKET GYPSIES 22 (1975) (remarking that the average Eurodollar deposit ranges from \$1 million to \$5 million).

111. B. KETTELL, THE FINANCE OF INTERNATIONAL BUSINESS 219 (1981); F. MANN, *supra* note 101, at 195.

112. See J. LITTLE, *supra* note 110, at 23 (commenting that commercial banks own 80% of the Eurodollar deposits in London, the largest Eurodollar market); B. KETTELL, *supra* note 111, at 218 (stating that the Eurodollar market is principally an interbank market). Other depositors in the Eurocurrency market include central banks, government bodies, large corporations and affluent individuals. M. STIGUM, *supra* note 30, at 113.

113. See *Libyan Arab Foreign Bank v. Bankers Trust Co.*, [1986] L. No. 1567/L. No. 4048 (Q.B.) 40-42, *reprinted in* 26 I.L.M. 1600, 1623-24 (1987) (assuming the Eurodollar nature of the LAFB's London account).

114. *Libyan Arab Foreign Bank v. Bankers Trust Co.*, [1986] L. No. 1567 (C.A.) 7.

115. *Id.*

LAFB never effected any payments into or withdrawals from its London account using checks.¹¹⁶ Bankers Trust Company, therefore, had little difficulty in establishing that at all relevant times, the LAFB's London account was a Eurodollar account.

Having decided that the LAFB's London account was within the scope of the international Eurodollar market, the British court next examined the customs and usages in the operation of the Eurodollar market governing the repayment obligations of Eurobanks.¹¹⁷ When funds are held in a Eurodollar account, repayment will generally occur only within the monetary system of the country issuing the currency, that is, the United States.¹¹⁸ To receive payment from a Eurodollar account, the LAFB must instruct Bankers Trust Company in London to make payments to a specific account in its correspondent bank in the United States.¹¹⁹ In turn, the Society for Worldwide Interbank Financial Transfers (SWIFT)¹²⁰ will instruct Bankers Trust Company in New York to move funds from its correspondent account held for its foreign branch to the Libyan nominated correspondent bank account in the United States.¹²¹ The actual transfer of funds is effected through the United States domestic clearing system for international payments, CHIPS, located in New York.¹²² Consequently, the transfer is effected

116. *Libyan Arab Foreign Bank v. Bankers Trust Co.*, [1986] L. No. 1567/ L. No. 4048 (Q.B.) 1, *reprinted in* 26 I.L.M. 1600, 1600 (1987).

117. *Id.* at 40-44.

118. Carreau, *supra* note 67, at 161; *see* Mann, *Zahlungsprobleme bei Fremdwährungsschulden (Payment Problems in Connection with Foreign Currency Debts)*, 36 ANNUAIRE SUISSE DE DROIT INT'L 93, 98-99 [hereinafter *Payment Problems*] (remarking that the place of repayment of a Eurodollar contract is in New York).

119. Hoffman & Giddy, *supra* note 7, at 78.

120. *See* ELECTRONIC TRANSFER SYSTEMS, *supra* note 78, §§ 9.01, 9.05 (noting that SWIFT serves exclusively as a telecommunication network facilitating multicurrency payments messages between participating banks). SWIFT does not participate in the settlements of various bank transactions. *Id.* SWIFT is a privately owned cooperative society in Belgium. *Id.*

121. Hoffman & Giddy, *supra* note 7, at 78.

122. *Id.* CHIPS is an automated facility processing more than 90% of interbank transfers of dollars daily. ELECTRONIC TRANSFER SYSTEMS, *supra* note 78, § 9.04. As of December 1984, there were 133 CHIPS participants. D. BAKER & R. BRANDEL, THE LAW OF ELECTRONIC FUND TRANSFER SYSTEMS § 9.04 (Supp. 1985). Twenty-one of these participants were designated as clearing or settlement banks for Eurodollar deposits. *Id.* To participate in CHIPS, nonclearing members must enter an agreement with a settling member bank. *Id.*; *see* Roussakis, *Evolution of International Banking and its U.S. Development*, in INTERNATIONAL BANKING 34-36 (E. Roussakis ed. 1983) [hereinafter *Evolution of International Banking*] (tracing the evolution of CHIPS as the premier settlement mechanism for Eurodollar transactions); Delbruk & Co. v. Manufactures Hanover Trust Co., 464 F. Supp. 989, 992-93 (S.D.N.Y.), *aff'd*, 609 F.2d 1047 (2d Cir. 1979) (describing the operation of CHIPS that allows correspondent banks to offset inpayments and outpayments among themselves).

on the same business day the instruction is sent,¹²³ and settlement is made between the banks in federal funds.¹²⁴ At the end of each business day, the Federal Reserve Bank will adjust the Libyan and New York Bankers Trust Company reserve accounts.¹²⁵ Therefore, because Eurodollar transactions are ultimately cleared through the CHIPS mechanism in the United States, the repayment of Eurodollar deposits requires that some transactions occur in the United States.¹²⁶

If Bankers Trust Company is to honor the LAFB's demand for repayment of the London Eurodollar account, it must use the CHIPS mechanism located in the United States.¹²⁷ Using the CHIPS mechanism would require actions in violation of the Libyan Sanctions Regulations.¹²⁸ Under the laws of the United Kingdom, however, a party is properly excused from performing a contractual obligation if the performance involves actions in a forum where the actions are illegal.

In *Ralli Brothers v. Compania Naviera Sota y Aznar*,¹²⁹ the English court examined the illegality defense and declined to order the defendant to perform an act in a foreign state that violated the laws of that state.¹³⁰ A charter agreement between the defendant, an English firm,

123. *Evolution of International Banking*, *supra* note 122, at 34. A central CHIPS computer managing the transfer of funds will debit a specified amount from the correspondent bank account of the London-Bankers Trust and will credit the nominated Libyan correspondent bank account with that equivalent amount. R. GOODE, *PAYMENT OBLIGATIONS IN COMMERCIAL AND FINANCIAL TRANSFERS* 101 (1983) [hereinafter *PAYMENT OBLIGATIONS*]; M. STIGUM, *supra* note 30, at 434-35.

124. *Evolution of International Banking*, *supra* note 122, at 34. Federal funds are deposit balances of financial institutions held with Federal Reserve banks. *Id.*

125. *PAYMENT OBLIGATIONS*, *supra* note 123, at 97. The Federal Reserve Bank maintains an escrow account to accumulate and disburse settlement payments. D. BAKER & R. BRANDEL, *supra* note 122, § 9.04. Using a CHIPS report calculating in payments and outpayments between settling banks, the member banks use CHIPS to settle accounts with each other at the end of the business day via transfers through the Federal Reserve account using Fedwire. *Id.*

126. *Libyan Arab Foreign Bank v. Bankers Trust Co.*, [1986] L. No. 1567/L. No. 4048 (Q.B.) 41-42, *reprinted in* 26 I.L.M. 1600, 1623-24 (1987). During the trial, Bankers Trust Company presented expert testimony noting that all participants in the Eurodollar market recognized the market as strictly a noncash market and that all Eurodollar transactions, except those involving a movement of funds from one account at a given bank to another account at that same bank, are cleared in the United States. *Id.* at 42.

127. *See id.* (explaining that with one minor exception, all Eurodollar transactions are cleared in the United States). The one minor exception, known as an in-house transfer, would require the London branch of Bankers Trust Company to transfer the balance of the LAFB's account to a beneficiary the LAFB nominated, who also has an account with the London branch. *Id.* at 32. The LAFB, however, did not want to benefit any other institution with an account at the London branch. *Id.* at 46.

128. *Financial Times*, Dec. 3, 1986, at 9, col. 1.

129. *Ralli Brothers v. Compania Naviera Sota y Aznar*, [1920] 2 K.B. 287.

130. *Id.* at 292. A British court recently examined the illegality defense. *XAG Bank v. A. Bank*, 2 All E.R. 464, 467 (1983). In *XAG Bank*, the United States District

and the plaintiff, a Spanish company, for a voyage from Calcutta to Barcelona contemplated payment for freight in the amount of fifty pounds at the port of destination.¹³¹ When the vessel arrived in Barcelona, the parties discovered that a Spanish decree made it illegal for shippers or carriers to pay or receive more than 875 pesetas per ton of freight.¹³² The English charterers, therefore, refused to pay any amount in excess of 875 pesetas to the Spanish shipowners, a fraction of the fifty pounds due under the original agreement.¹³³

The English court, exhibiting a marked deference to Spanish law, held that the English shipper did not have to pay the Spanish owners any amount in excess of the 875 pesetas per ton of freight allowed under Spanish law.¹³⁴ The court accepted the principle that "a contract is invalid if its performance becomes unlawful under the law of the country where performance is required."¹³⁵ Thus, no civilized state

Court for the Southern District of New York served a subpoena on *A* bank, a foreign branch of a United States bank, requiring production of books, records, and other documents relating to the accounts of *X*, *A*, and *G*. *Id.* The subpoena noted that the court would subject the bank to contempt of court and penalties if it did not comply with the subpoena. *Id.* at 470. Subsequently, the plaintiffs sought an injunction to prohibit defendants from producing documents relating to their accounts. *Id.* at 467. Defendants argued that a British court's injunction would require it to perform an unlawful act violating New York law. *Id.* at 470.

The British court granted an injunction, holding that the bank owed a duty of confidentiality to plaintiffs prohibiting production of documents relating to the accounts of *X*, *A*, and *G*. *Id.* at 480. The British court took the position that unless a United States legislative decree or judgment ordered disclosure of these documents, the bank would not violate United States law in maintaining secrecy. *Id.* at 465. Moreover, if the bank presented a sufficient excuse to the United States District Court for not producing the documents, the court would excuse it from releasing the documents. *Id.* Thus, the English court held that the United States should refrain from imposing the sanction of contempt on the *A* bank complying with its duty of confidentiality owed to *XAG*. *Id.*

Under this analysis, the British court should recognize Libyan sanctions regulations prohibiting repayment of the Eurodollar account. The United States regulations impose penalties on United States persons if they permit any withdrawal of dollar-denominated deposits unless a license has been obtained. 31 C.F.R. §§ 550.209, 550.701 (1987). Because the United States must clear the Bankers Trust Company's repayment of the LAFB's Eurodollar account, the British court's failure to excuse its performance will result in the Bankers Trust Company violating the Libyan Sanctions Regulations. *Libyan Arab Foreign Bank v. Bankers Trust Co.*, [1986] L. No. 1567/L. No. 4048 (Q.B.) 3, 40, reprinted in 26 I.L.M. 1600, 1604, 1623 (1987).

131. *Ralli Brothers v. Compania Naviera Sota y Aznar*, [1920] 2 K.B. 287, 288-90.

132. *Id.* at 290.

133. *Id.*

134. *Id.* at 292.

135. *Id.* at 291. One can interpret *Ralli Brothers v. Compania Naviera Sota Y Aznar* as accepting certain maxims on the meaning of impossibility of performance. The first and most widely accepted maxim is that impossibility of performance depends on the law where the contract is performed. *Payment Problems*, *supra* note 118, at 104. Second, another formulation of the decision in *Ralli Brothers* is that the statute of

should force a debtor to make a payment that is a punishable offense at the place of payment.¹³⁶ Consequently, the English court released the English debtor from repaying the excess amount due under the contract.¹³⁷

The decision in *Libyan Arab Foreign Bank v. Bankers Trust Co.*¹³⁸ does not retreat from this well accepted legal principle. Bankers Trust Company argued that the practice of the international Eurodollar market gave rise to an implied term requiring repayment of the LAFB's Eurodollar account through the CHIPS mechanism located in the United States.¹³⁹ Repayment in this manner would require Bankers Trust Company to violate the Libyan Sanctions Regulations.¹⁴⁰ Bankers Trust Company, therefore, argued that the principles derived from the *Ralli Brothers* case should excuse its refusal to honor the LAFB's demands for repayment.¹⁴¹

Both the LAFB and Bankers Trust Company presented expert testimony concerning the established practices of the international Eurodollar market.¹⁴² The court, after weighing the evidence, concluded that the LAFB had presented the more compelling evidence.¹⁴³ The court

debt determines whether or not impossibility under the law of the place of performance exists. *Id.* Finally, the decision in *Ralli Brothers* may mean that a debtor is discharged from performing under the contract if the law of the place of performance deems such performance an impossibility. *Id.*

136. *Payment Problems*, *supra* note 118, at 104.

137. *Ralli Brothers v. Compania Naviera Sota y Aznar*, [1920] 2 K.B. 287, 292; see *Payment Problems*, *supra* note 118, at 105 (noting that the consequences of releasing a debtor from payment of a monetary obligation is legally unacceptable). One monetary analyst has noted that the performance of a money debt is never impossible. F. MANN, *supra* note 101, at 421. The debtor and the creditor may reach an agreement changing the place of repayment of a money debt, thereby circumventing exchange restrictions. *Id.* Moreover, the creditor could also refrain from demanding immediate payment of a money debt. *Id.* If a Eurodollar contract has expressly or impliedly specified that repayment of a Eurodollar deposit must proceed through CHIPS, then the parties should always anticipate that repayment may become impossible under this system. *Id.* at 420. According to one monetary scholar, if payment should become temporarily suspended under the CHIPS system, then the obligation of the English bank is only temporarily suspended. *Id.*

138. *Libyan Arab Foreign Bank v. Bankers Trust Co.*, [1986] L. No. 1567/L. No. 4048 (Q.B.), reprinted in 26 I.L.M. 1600 (1987).

139. *Id.* at 40.

140. *Id.* at 3.

141. See *id.* at 19 (stating that the performance of contractual obligations is excused when performance necessarily requires doing an act that is unlawful under the laws of the place where it must be done).

142. *Id.* at 41.

143. *Id.* at 42. Additionally, the course of dealings between the parties from December 1980 to January 1986 was contrary to an implied term requiring clearing all transactions through the CHIPS mechanism in the United States. *Id.* at 43. Even though a large percentage of the LAFB's transactions involving the London account were cleared through the CHIPS mechanism, that mechanism was not exclusive. *Id.*

declined to imply a term into the deposit contract making use of the CHIPS mechanism the exclusive means through which Bankers Trust Company could meet the LAFB's repayment demands.¹⁴⁴ Having rejected Bankers Trust Company's Eurodollar defense, the court considered the additional mechanisms Bankers Trust Company could use to comply with the LAFB's demand for repayment,¹⁴⁵ and considered whether these mechanisms would require some actions in the United States in violation of the Libyan Sanctions Regulations.¹⁴⁶ The court ultimately concluded that Bankers Trust Company could honor the LAFB's demands for repayment through the delivery of an appropriate sum of United States dollars to the LAFB in London.¹⁴⁷ This method of repayment, the court reasoned, would not involve any illegal actions in the United States.¹⁴⁸ The court, therefore, found that because honoring the LAFB's demands for repayment of the London Eurodollar account was not illegal under the proper substantive law governing the deposit contract and did not require actions in a forum where such actions are illegal, Bankers Trust Company was liable.¹⁴⁹

II. THE BRETTON WOODS DEFENSE

The previous section analyzed the customs and practices of the international Eurodollar market and whether those practices gave rise to an implied contractual term that would effectively defeat the LAFB's demand for repayment of its London Eurodollar account. Rather than concentrate on the specific facts of the Libyan litigation, Part II outlines a public international law defense available to commercial banks defending against depositors seeking repayment of frozen Eurodollar

144. *Id.*

145. *See id.* at 32-37 (listing the various methods Bankers Trust Company could use to honor the LAFB's demand for repayment).

146. *See id.* at 46-55 (examining whether each of the various forms of repayment Bankers Trust Company can use would even remotely raise the possibility of involving the mechanisms of the United States commercial banking system).

147. *Id.* at 51. Alternatively, if United States dollars are unavailable, the LAFB is entitled to demand payment in sterling. *Id.* at 54. Generally, banks participating in the Eurodollar market do not settle transactions in cash. PAYMENT OBLIGATIONS, *supra* note 123, at 91; Effros, *supra* note 87, at 642. Where a depositor is withdrawing a large amount of money, as the LAFB was, payment in cash is both risky and cumbersome. PAYMENT OBLIGATIONS, *supra* note 123, at 91. The court, after recognizing the commercial impracticalities of a cash payment, chose to ignore the factors rendering a cash payment extremely troublesome. *Libyan Arab Foreign Bank v. Bankers Trust Co.*, [1986] L. No. 1567/L. No. 4048 (Q.B.) 50-51, *reprinted in* 26 I.L.M. 1600, 1628 (1987).

148. *Libyan Arab Foreign Bank v. Bankers Trust Co.*, [1986] L. No. 1567/ L. No. 4048 (Q.B.) 51, *reprinted in* 26 I.L.M. 1600, 1628 (1987).

149. *Id.*

accounts. This section examines the analytic structure of article VIII, section 2(b) of the Articles of Agreement of the International Monetary Fund, reviews the various interpretations of article VIII, section 2(b) followed in the United States and Europe, and concludes that in jurisdictions adhering to a broad interpretation of article VIII, section 2(b), the IMF defense is a viable alternative available to commercial banks defending against depositors seeking repayment of frozen Eurodollar accounts.

A. THE INTERNATIONAL MONETARY FUND

The IMF is a specialized agency of the United Nations that functions as an independent international organization regulating countries in matters affecting their currencies or balance of payments.¹⁵⁰ Applicable regulations and statements setting forth the general purposes of the IMF are contained in the Articles of Agreement of the International Monetary Fund which were formally adopted at the Bretton Woods Conference in 1944.¹⁵¹ Article I¹⁵² of the Articles of Agreement lists purposes relative to article VIII, section 2(b), including duties to eliminate foreign exchange restrictions hampering world trade, duties to maintain orderly exchange arrangements among members, and duties to promote international monetary cooperation through a permanent institution permitting consultation or collaboration on international monetary conflicts.¹⁵³ Many courts set forth these stated purposes of the IMF in their decisions to support either a narrow or a broad interpretation of article VIII, section 2(b).¹⁵⁴

150. Gold, *The International Monetary Fund*, in A LAWYER'S GUIDE TO INTERNATIONAL BUSINESS TRANSACTIONS 7, 8 (W. Surrey & D. Wallace Jr. 2d ed. 1979) [hereinafter *The IMF*]; see J. HORSEFIELD, INTRODUCTION TO THE FUND 4-18 (IMF Pamphlet Series No. 1, 2d ed. 1965) (providing representative examples of the IMF supervising par value, convertibility, and stand-by and quota arrangements among its members).

151. *The IMF*, *supra* note 150, at 9.

152. Agreement, *supra* note 24, art. I.

153. *Id.* Other purposes of the IMF mentioned in article I include: duties to facilitate the expansion of international trade, duties to make the general resources of the IMF temporarily available to its members so they can correct maladjustments in their balance of payments without reliance on measures destructive of national or international prosperity, and duties to assist in the establishment of a multilateral system of payments in respect of current transactions between members. *Id.*

154. See *Wilson, Smithett & Cope Ltd. v. Terruzzi*, [1976] 1 Q.B. 683, 709 (C.A.) (noting one purpose of the IMF, the promotion of international trade, supports a narrow interpretation of article VIII, section 2(b)); see also *Lessinger v. Mirau*, 22 I.L.R. 725, 726 (Oberlandesgericht, Schleswig-Holstein 1954) (implying that another purpose of the Fund, promoting cooperation of members with respect to exchange control regulations of their fellow members, supports a broad interpretation of article VIII, section 2(b)).

1. *Structure of the Membership*

The IMF is composed of both original members, those countries represented at the United Nations Monetary and Financial Conference whose governments accepted membership before December 31, 1945, and countries accepting membership after 1945.¹⁵⁵ Resolutions of the IMF Board of Governors establish the terms and conditions of membership for these countries.¹⁵⁶ One requirement of membership is that member countries respect the Articles of Agreement and undertake general obligations under articles IV¹⁵⁷ and VIII¹⁵⁸ of the Articles of Agreement.¹⁵⁹ The IMF may publicly sanction any member that fails to observe the obligations imposed under these articles.¹⁶⁰ The IMF may also sanction a member in an informal manner.¹⁶¹ Consequently, most member countries observe their obligations, recognizing that penalties and public sanctions may adversely affect their positions in the IMF and among various countries individually.¹⁶²

An additional general obligation of all members is found in article VIII, section 2(b).¹⁶³ Article VIII, section 2(b) imposes restrictions on all exchange contracts involving IMF members.¹⁶⁴ The article states, in

155. Agreement, *supra* note 24, art. II.

156. The IMF, *supra* note 150, at 9; see Gold, *Australia and Article VIII, Section 2(b) of the Articles of Agreement of the International Monetary Fund*, 57 AUSTL. L.J. 560, 561 (1983) (discussing the requirements imposed on countries applying for membership in the IMF).

157. Agreement, *supra* note 24, art. IV. Article IV requires members to collaborate with the IMF and other members to assure orderly exchange arrangements and promote a stable system of exchange rates. *Id.*

158. Agreement, *supra* note 24, art. VIII. Under article VIII, section 3, members have a general obligation to avoid discriminatory currency arrangements or multiple currency practices. *Id.*

159. Agreement, *supra* note 24, arts. IV, VIII.

160. See J. GOLD, LEGAL INSTITUTIONAL ASPECTS OF THE INTERNATIONAL MONETARY SYSTEM 153-54 (J. Everson & J. Oh 2d ed. 1979) [hereinafter LEGAL AND INSTITUTIONAL ASPECTS] (noting that the IMF, upon a special two-thirds majority vote, may publish a report made to a member who violates article XII, section 8).

161. See Agreement, *supra* note 24, art. XII (discussing the right of the fund to communicate its views informally to a member on any matter arising under the Articles of Agreement); see also Gold, *Certain Aspects of the Law and Practice of the International Monetary Fund*, in THE EFFECTIVENESS OF INTERNATIONAL DECISIONS 71 (S. Schwebel ed. 1971) (describing the process of communicating the views of the IMF Managing Director and his or her staff to breaching members under an informal arrangement).

162. LEGAL AND INSTITUTIONAL ASPECTS, *supra* note 160, at 178.

163. Agreement, *supra* note 24, art. VIII. Members are also expected to cooperate in making the exchange control regulations of other members more effective if such measures and regulations are consistent with the Agreement under article VIII, section 2(b). *Id.*

164. *Id.*

pertinent part: "[E]xchange contracts which involve the currency of any member and which are contrary to the exchange control regulations of that member maintained or imposed consistently with this Agreement shall be unenforceable in the territories of any member."¹⁶⁵ Defining a Eurodollar deposit arrangement as an exchange contract involving United States dollars allows United States banks defending against claims for repayment of frozen Eurodollar accounts to argue that repayment is contrary to a United States asset freeze, which is an exchange control regulation imposed consistently with the IMF Agreement.¹⁶⁶ Applying article VIII, section 2(b), a United States bank must prove four elements: 1) that the Eurodollar arrangement constitutes an exchange contract; 2) that the Eurodollar arrangement involves United States currency; 3) that the Eurodollar arrangement contradicts a United States exchange control regulation, an asset freeze in this case; and 4) that the exchange control regulation is consistent with the IMF Agreement. If the defending commercial bank proves all four elements of the IMF defense, courts in all IMF member states, including the United Kingdom, must honor a United States asset freeze and refrain from ordering the performance of a Eurodollar contract.¹⁶⁷

a. Eurodollar Arrangements as Exchange Contracts

The IMF has never precisely defined an exchange contract, but various courts of member countries have interpreted the term.¹⁶⁸ These courts have developed both a narrow and a broad interpretation of exchange contracts under article VIII, section 2(b). The narrow or literal interpretation states that an exchange contract has as its immediate purpose the exchange of one currency for another.¹⁶⁹ The broad inter-

165. *Id.*

166. See *Bank Markazi Iran v. Manufacturers Hanover Trust Co.* [1979] L. No. 5907 (Q.B.) 6 (raising the IMF argument during the Iranian litigation in London).

167. Edwards, *supra* note 9, at 881; see *SELECTED DECISIONS*, *supra* note 27, at 251 (stating that if the requirements of article VIII, section 2(b) are fulfilled, judicial authorities of member countries should not assist other members through awarding damages for the nonperformance of exchange contracts).

168. See Baker, *Enforcement of Contracts Violating Foreign Exchange Control Laws*, 3 INT'L TRADE L.J. 247, 253 (1977) (analyzing how the courts of several European nations and the United States have interpreted article VIII, section 2(b)).

169. Nussbaum, *Exchange Control and the International Monetary Fund*, 59 YALE L.J. 395, 426 (1950) (stating the narrow interpretation of an exchange contract for the first time); see *Frantzmann v. Ponijen*, 30 I.L.R. 423, 423 (Neth., D. Ct. Maastricht 1966) (applying the literal interpretation of an exchange contract and holding a loan contract unenforceable under article VIII, section 2(b)). In *Frantzmann v. Ponijen*, the plaintiff and defendant, both residents of Indonesia, entered into a loan agreement requiring the plaintiff to pay the defendant in Indonesian rupiahs. *Id.* In return, the defendant agreed to repay the plaintiff Dutch guilders in Holland. *Id.* When

pretation defines an exchange contract as a contract that affects the exchange resources of the member country imposing the restrictions.¹⁷⁰ Consequently, it is substantially more difficult to categorize a Eurodollar arrangement as an exchange contract under the narrow definition than it is under the broader definition.

The United States¹⁷¹ and the United Kingdom,¹⁷² in adopting the narrow definition of an exchange contract, have focused on the specific object of the contractual agreement. In *Wilson Smithett & Cope Ltd. v. Terruzzi*,¹⁷³ the English Court of Appeal definitively stated that an exchange contract is a contract to exchange the currency of one country for the currency of another.¹⁷⁴ In *Terruzzi*, the plaintiff, a dealer on the London metal exchange, extended credit to Terruzzi, an Italian res-

the defendant made only partial repayment on the loan, the plaintiff sued for the balance. *Id.* The District Court, applying a literal interpretation of an exchange contract, held that the loan contract was an exchange contract calling for an exchange of rupiahs for guilders. *Id.* See generally Williams, *Extraterritorial Enforcement of Exchange Control Regulations Under the International Monetary Fund Agreement*, 15 VA. J. INT'L L. 319, 337 (1975) [hereinafter *Extraterritorial Enforcement*] (noting that one legal scholar, abandoning the literal interpretation, believes that an exchange contract exists only where a party promises to pay money in the currency of the country imposing the restrictions).

170. J. GOLD, *THE FUND AGREEMENT IN THE COURTS* II 393 (1983) [hereinafter *COURTS II*]; see Mann, *The Private International Law of Exchange Control Under the International Monetary Fund Agreement*, 2 INT'L & COMP. L.Q. 97, 102 (1953) (advocating that a broad interpretation of an exchange contract facilitates and supports the economic purposes of the IMF).

171. See *Banco do Brasil, S.A. v. A.C. Israel Commodity Co.*, 12 N.Y.2d 371, 375-76, 190 N.E.2d 235, 236-37, 239 N.Y.S.2d 872, 873-74 (1963), *cert. denied*, 376 U.S. 906 (1964) (following the narrow interpretation of an exchange contract and ignoring the economic goals of the IMF); see also *Libra Bank Ltd. v. Banco Nacional de Costa Rica*, 570 F. Supp. 870, 900 (S.D.N.Y. 1983) (holding that a loan contract requiring repayment in United States dollars, the currency of the loan, is not an exchange contract). But see *Banco Frances e Brasileiro S.A., v. Doe*, 36 N.Y.2d 592, 598, 331 N.E.2d 502, 506, 370 N.Y.S.2d 534, 539 (1975) (applying the broad definition of an exchange contract and enforcing currency controls of a friendly nation). At times, however, United States courts have failed to give any meaningful definition of an exchange contract. Williams, *Foreign Exchange Control Regulation and the New York Court of Appeal: J. Zeevi & Sons Ltd. v. Grindlays Bank (Uganda) Ltd.*, 9 CORNELL INT'L L.J. 239, 243 (1976). Even though the contract in question, labeled as a letter of credit, fell within the narrow definition of an exchange contract, the court held that such a letter of credit was not an exchange contract. *J. Zeevi & Sons Ltd. v. Grindlays Bank (Uganda) Ltd.*, 37 N.Y.2d 220, 229, 333 N.E.2d 168, 371 N.Y.S.2d 892, 900, *cert. denied*, 423 U.S. 866 (1975).

172. *Wilson, Smithett & Cope Ltd. v. Terruzzi*, [1976] 1 Q.B. 683, 709-14 (C.A.). The House of Lords upheld this holding. *United City Merchants v. Royal Bank of Canada*, 1 App. Cas. 188 (1983). The English Court of Appeal, however, originally adopted a broad definition of exchange contracts. *Sharif v. Azad*, [1967] 1 Q.B. 605 (C.A.). Lord Diplock held that courts should liberally construe exchange contracts to protect the financial resources of a country. *Id.* at 618.

173. *Wilson, Smithett & Cope Ltd. v. Terruzzi*, [1976] 1 Q.B. 683 (C.A.).

174. *Id.* at 714.

ident dealing in metals.¹⁷⁵ Terruzzi instructed the plaintiff to sell short 1200 tons of zinc for three months delivery.¹⁷⁶ The price of zinc rose substantially, and the plaintiff demanded a deposit from the defendant in accordance with the terms of the contract.¹⁷⁷ When Terruzzi refused to honor this demand, the plaintiff closed the account, selling the metal back to the defendant at the prevailing market price.¹⁷⁸ The English Court of Appeal entered a judgment for the plaintiff for the costs of covering a short sale.¹⁷⁹

The British Court of Appeal, refusing to adopt a broader interpretation of the term "exchange contract," dismissed Terruzzi's allegation that the contract affected the exchange resources of Italy.¹⁸⁰ Noting that the contract only called for payment in sterling, the court concluded that the contract was not an exchange contract contemplating an exchange of currencies.¹⁸¹ This narrow reading of the term "exchange contract" implies that most financial transactions do not fall within the scope of article VIII, section 2(b).¹⁸² The English court also rejected the defendant's argument that transactions involving merchandise or commodities are classified as exchange contracts.¹⁸³ The court

175. *Id.* at 709-10. Under Italian exchange control laws, no Italian resident could incur debts to nonresidents without ministerial authority. *Id.* at 710. Terruzzi did not obtain such permission before establishing an account with Wilson, Smithett & Cope Ltd. *Id.*

176. *Id.* The court explained that Terruzzi sold metal that he did not have to London dealers at a high price for delivery three months later. *Id.* He never intended to deliver, but rather wanted to buy a similar quantity back from the London dealers at a lower price before the delivery date. *Id.*

177. *Id.*

178. *Id.* at 711. Upon the satisfaction of the sale to Terruzzi, a debt of 195,000 pounds sterling still remained on the account. *Id.*

179. *Id.*

180. *Id.* at 714 (dismissing the appeal because the contracts were not exchange contracts but rather contracts, for the sale and purchase of metal).

181. *Id.*

182. See COURTS II, *supra* note 170, at 393 (explaining that forward exchange contracts where one party promises to exchange one currency for another constitute one of the few financial transactions included within the scope of a narrow interpretation of the term exchange contract); see also Gold, "Exchange Contracts" *Exchange Control, and the IMF Articles of Agreement: Some Animadversions on Wilson, Smithett & Cope Ltd. v. Terruzzi*, 33 INT'L & COMP. L.Q. 777, 786 (1984) [hereinafter Gold, *Some Animadversions on Wilson, Smithett & Cope Ltd. v. Terruzzi*] (noting that a loan agreement where one party lends money in return for repayment in the same currency is excluded from the definition of an exchange contract under a literal interpretation); Rendell, *The Allied Bank Case and its Aftermath*, 20 INT'L LAW. 819, 827 (1986) (remarking that a promissory note is not classified as an exchange contract under a restrictive formulation of the term).

183. *Wilson, Smithett & Cope Ltd. v. Terruzzi*, [1976] 1 Q.B. 683, 713 (C.A.). The court noted that the IMF enacted article VIII, section 2(b) to curb the evil of currency speculation. *Id.* at 713. Contracts for the sales of merchandise or commodities did not cause this evil. *Id.* The court held that the Bretton Woods Agreement pre-

did, however, create a narrow exception for commodities contracts that are, in effect, disguised monetary transactions for the exchange of currencies.¹⁸⁴

In *United City Merchants v. Royal Bank of Canada*,¹⁸⁵ the House of Lords, applying the narrow exception, examined the underlying substance of a sales transaction and discovered a disguised monetary transaction involving an exchange of currencies violating Peruvian exchange control regulations.¹⁸⁶ Glass Fibres and Equipment Ltd. (Glass Fibres), an English company, sold a plant to Vitrorefuerzos (Vitro), a Peruvian company, for \$662,086.¹⁸⁷ The buyer arranged for its Peruvian bank, Banco Continental, S.A., to supply an irrevocable letter of credit confirmed at the Royal Bank of Canada (Royal Bank).¹⁸⁸ Glass Fibres and Vitro, however, devised a scheme requiring Glass Fibres to sell the

cluded any restrictions on valid commodities or sales contracts and stressed the promotion of international trade under article I (ii). *Id.* Article VI, section 3 and article VIII, section 2(a), coupled with article XIX(1), prohibits any IMF member from imposing restrictions on payments "due in connection with foreign trade, other current business, including services, and normal short term banking credit facilities." *Id.* at 713-14.

The IMF, however, can approve a member's restrictions on current international trade transactions under article VIII, section 2(a), but the court of appeal took the position that only minimal restrictions are in the interests of trade. Gold, *Some Animadversions on Wilson, Smithett & Cope Ltd. v. Terruzzi*, *supra* note 182, at 802-03. The rationale of the Court of Appeal lacks merit because it failed to meaningfully consider the tenets of articles I (ii), (v), and (vi). These tenets include the following provisions: promoting international monetary collaboration, establishing confidence in members through allowing them to correct maladjustments in their balance of payments, and lessening the degree of disequilibrium in the balance of payments of member countries. Agreement, *supra* note 24, art. I (ii), (v), (vi). The Court of Appeal conducted a cursory analysis of these tenets, concluding that their primary objective was the promotion of trade. F. MANN, *supra* note 101, at 388. A short-term, IMF-approved trade restriction promotes these additional tenets. COURTS II, *supra* note 170, at 217.

184. See *Wilson, Smithett & Cope Ltd. v. Terruzzi*, [1976] 1 Q.B. 683, 718 (C.A.) (citing Nussbaum as arguing that contracts involving securities or merchandise are not exchange contracts, unless they are monetary transactions in disguise); see Nussbaum, *supra* note 169, at 427 (containing the original statement of this exception and noting that sales or commodities contracts are enforceable even if they are illegal under the law of the country of the currency); see also F. MANN, *supra* note 101, at 388 (discussing how the definition of "contracts in disguise" distorts reality and creates uncertainty).

185. *United City Merchants v. Royal Bank of Canada*, [1983] 1 App. Cas. 168, 188.

186. *Id.* at 188, 190.

187. *Id.* at 180-81.

188. *Id.* at 181. A documentary credit is any arrangement where a bank, acting on the request or instructions of a customer or applicant for credit, either 1) makes a payment to, or to the order to, a third party or is to pay or accept bills of exchange drawn by the beneficiary, or 2) authorizes another bank to do so, against certain documents, provided that the parties comply with the terms of the credit. *Uniform Customs and Practice for Documentary Credits*, art. 2 (Int'l Chamber of Commerce No. 400, 1983).

plant to Vitro at twice the actual cost.¹⁸⁹ Glass Fibres, after receiving the inflated amount of United States currency, would then remit half of the amount received to the subsidiary of Vitro located in Miami, Florida.¹⁹⁰ This scheme would have allowed Vitro to convert Peruvian soles into United States dollars in violation of Peruvian exchange control regulations.¹⁹¹ The Royal Bank, however, refused to honor a call on the letter of credit supplied pursuant to the sales contract.¹⁹²

United City Merchants (UCM), an assignee of the rights of Glass Fibres under the letter of credit, sued Royal Bank for payment.¹⁹³ Royal Bank argued that the sales contract was unenforceable under article VIII, section 2(b) because it was an exchange contract.¹⁹⁴ The House of Lords agreed with Royal Bank, allowing UCM to recover on the part of the contract representing the true purchase price of the equipment, but refused to allow UCM any recovery for that part of the transaction in excess of the genuine purchase price.¹⁹⁵ This part of the contract represented the disguised monetary transaction.¹⁹⁶ The significance of this decision is two-fold. First, the House of Lords recognized the necessity of relying on the substance rather than the form of a contract in determining whether the contract is designed to evade the exchange control regulation of an IMF member.¹⁹⁷ Second, the House of Lords acknowledged that courts may merge a series of related contractual arrangements¹⁹⁸ and conclude that the series constitutes a single

189. *United City Merchants v. Royal Bank of Canada*, [1983] 1 App. Cas. 168, 182.

190. *Id.*

191. *Id.*

192. *Id.* at 181-82. The letter of credit required that a carrier ship all goods on or before December 15, 1976. *Id.* at 181. The carrier subsequently shipped the goods on December 16, 1976. *Id.* The carrier's agent, however, presented fraudulently backdated bills of lading to Royal Bank, the confirming bank, without the knowledge of the sellers. *Id.* at 181-82.

193. *Id.* at 170-71.

194. *Id.* at 178.

195. *Id.* at 190.

196. *Id.*

197. *Id.* at 188. If the House of Lords limited its review to the form of the contract between Glass Fibres and Royal Bank under the documentary credit, it would not have labeled the contract a currency exchange contract. *Id.* at 189-90.

198. *Id.* at 179. Lord Stephenson, of the British Court of Appeal, analyzed the case as encompassing four contractual relationships: 1) between Glass Fibres and Vitro for the sale and purchase of the plant; 2) between Vitro and Banco Continental (the buyer's Peruvian bank), who opened an irrevocable letter of credit benefitting Glass Fibres for the account of Vitro; 3) between Banco Continental and Royal, confirming the letter of credit; 4) between Royal and Glass Fibres, beneficiary under the letter of credit. *United City Merchants (Investments) Ltd. v. Royal Bank of Canada*, [1982] 1 Q.B. 208, 217.

exchange contract.¹⁹⁹ Consequently, the decision of the House of Lords suggests that contracts other than those concluded for an exchange of one currency for another may fall within the scope of article VIII, section 2(b).²⁰⁰

Many of the courts located in IMF member countries interpreting the meaning of an exchange contract under article VIII, section 2(b) have adopted a broader definition of exchange contracts. Courts in Germany²⁰¹ and France²⁰² define exchange contracts as those affecting the exchange resources of the member country imposing the restrictions, that is, a "contract which, when performed, would increase or decrease in an economic sense the amount of foreign exchange or other international reserves that are under the control of the country whose currency is involved."²⁰³ Under this broad interpretation, one commentator has suggested that exchange contracts are transactions that affect the international financial position of a country.²⁰⁴

In *Lessinger v. Mirau*,²⁰⁵ the German court of appeal accepted the broad interpretation of an exchange contract. The German court held that an exchange contract is a contract prejudicing the exchange resources of a member country.²⁰⁶ In *Mirau*, two Austrian citizens en-

199. *United City Merchants v. Royal Bank of Canada*, [1983] 1 App. Cas. 168, 179; Gold, *The Fund Agreement in the Courts - XIX*, 31 IMF STAFF PAPERS 179, 186 (1984). *Contra* F. MANN, *supra* note 101, at 389-90 (asserting that courts should not merge several contracts and conclude that, as a whole, they constitute a single exchange contract).

200. Note, *The Unenforceability of International Contracts Violating Foreign Exchange Regulations: Article VIII, Section 2(b) of the International Monetary Fund Agreement*, 25 VA. J. INT'L L. 967, 988 (1985).

201. See *Lessinger v. Mirau*, 22 I.L.R. 725, 725 (Oberlandesgericht, Schleswig-Holstein 1954) (holding that a loan agreement between two Austrian citizens is an exchange contract); Judgment of April 9, 1962, 21 WM 602 (Wertpapier mitteilunger) (holding that a contract for commission between German and Austrian manufacturers was an exchange contract); *Clearing Dollars Case*, 22 I.L.R. 730, 731 (Landgericht, Hamburg 1954) (defining an exchange contract as a contract involving the currency of an IMF member).

202. See *De Boer v. Ducro*, 47 I.L.R. 46, 51-52 (Cour d'appel, Paris 1961) (interpreting an assignment contract between a Dutch resident and a German resident as an exchange contract).

203. Williams, *supra* note 169, at 337-38. Contracts that increase or decrease foreign exchange or other international reserves at the time of their performance include contracts for the purchase or sale of merchandise or services, international loan agreements, and contracts for the exchange of one currency for another. Baker, *supra* note 168, at 253-54.

204. Silard, *Money and Foreign Exchange*, in 17 INT'L ENCY. COMP. L. 1, 58 (1975); see *De Boer v. Ducro*, 47 I.L.R. 46, 51 (Cour d'appel, Paris 1961) (analyzing the question of whether a contract affects a country's exchange resources).

205. *Lessinger v. Mirau*, 22 I.L.R. 725, 725 (Oberlandesgericht, Schleswig-Holstein 1954).

206. *Id.* at 727; see *De Boer v. Ducro*, 47 I.L.R. 46, 51 (Cour d'appel, Paris 1961)

tered into a contract requiring the defendant to pay 30,000 Austrian schillings in monthly installments to the plaintiff in exchange for a loan of an equivalent amount.²⁰⁷ The plaintiff loaned the defendant \$1,000 which is the equivalent of 30,000 Austrian schillings.²⁰⁸ When the defendant did not repay the loan, the plaintiff initiated suit to recover the \$1,000.²⁰⁹

At trial, the defendant raised article VIII, section 2(b), claiming that an exchange contract existed, and that if enforced, would violate Austrian exchange controls.²¹⁰ The German Court of Appeal, applying the broad interpretation of article VIII, section 2(b), refused to enforce the contract because the Austrian exchange control regulations prohibited the export of foreign exchange without a license, and the \$1,000 was illegally exported for the loan.²¹¹ Amounts of foreign exchange under Austrian control decreased as a result of this contract.²¹² Consequently, banks litigating the merits of a freeze affecting Eurodollar accounts in countries that adhere to the broad interpretation of article VIII, section 2(b) should find it easier to convince courts that a Eurodollar arrangement constitutes an exchange contract under article VIII, section 2(b).

The ability to fit a Eurodollar arrangement into the category of an exchange contract ultimately depends on the interpretive analysis the court selects. In jurisdictions adhering to the narrow interpretation of article VIII, section 2(b), a United States bank seeking to argue the IMF defense must integrate all related contracts of the Eurodollar arrangement into an underlying scheme and affirmatively demonstrate that the real objective is to exchange the currency of a depositor into United States dollars. In countries adopting the broader definition of

(asserting that the court must analyze a contract according to whether the contract will, in any way, affect the currency resources of the member imposing the exchange control regulations).

207. *Lessinger v. Mirau*, 22 I.L.R. 725, 725 (Oberlandesgericht, Schleswig-Holstein 1954).

208. *Id.*

209. *Id.* Because the defendant resided in the Federal Republic of Germany at the time the action commenced, the plaintiff sued for the Deutsch mark equivalent of \$1,000. *Id.*

210. *Baker*, *supra* note 168, at 254.

211. *Id.* at 254-55. The court defined an exchange contract as one affecting the exchange resources of the member implementing the exchange control regulations. *Lessinger v. Mirau*, 22 I.L.R. 725, 727 (Oberlandesgericht Schleswig-Holstein 1954). The German Court of Appeal noted that a broad interpretation of an exchange contract is the only interpretation consistent with the purposes behind controlling exchange resources. *Id.*

212. *Baker*, *supra* note 168, at 254; *see* J. GOLD, *THE FUND AGREEMENT IN THE COURTS* 91 (1962) [hereinafter *COURTS I*] (noting that the defendant was unable to return the amount borrowed to the Austrian government).

article VIII, section 2(b), however, a United States bank need only show that the Eurodollar transaction will have a cognizable effect on United States exchange resources or on the international financial position of the United States.

b. Eurodollar Arrangements as Involving United States Currency

The directors of the IMF have declined to interpret the meaning of an exchange contract, and they have never defined the phrase "involve the currency of a member."²¹³ Once again, courts of member states have developed their own interpretations. Not surprisingly, interpretations of this phrase correspond directly with the interpretations accorded exchange contracts.²¹⁴

In defining the phrase "involve the currency of a member," the first question to examine is whether a Eurodollar qualifies as United States currency. Technically, a Eurodollar is neither a coin nor a note.²¹⁵ Instead, a Eurodollar is simply a dollar-denominated bank deposit located outside the United States. Some commentators have argued, therefore, that a Eurodollar does not constitute United States currency.²¹⁶ Consequently, commercial banks claiming that a Eurodollar arrangement does involve United States currency, should argue that although a Eurodollar is not currency in the common sense, the Eurodollar arrangement does involve United States currency because the depositor has a claim to repayment in dollars or United States currency.²¹⁷

After defining what constitutes United States currency, it becomes necessary to determine what the term "involvement" means. Several courts have held that a currency is involved if the contract either explicitly names it the currency of repayment or performance of the contract necessarily requires payment of that currency.²¹⁸ Confusion, how-

213. R. EDWARDS, INTERNATIONAL MONETARY COLLABORATION 484, 486 (1985) [hereinafter COLLABORATION].

214. See COURTS II, *supra* note 170, at 214 (discussing limitations on the meaning of the phrase "involve the currency of a member" if a court supports a literal interpretation of an exchange contract).

215. PAYMENT OBLIGATIONS, *supra* note 123, at 2.

216. F. MANN, *supra* note 101, at 61; PAYMENT OBLIGATIONS, *supra* note 123, at 2.

217. See PAYMENT OBLIGATIONS, *supra* note 123, at 2 (explaining that a Eurodollar is a dollar deposit where the depositor has a claim to repayment in United States dollars).

218. See A. NUSSBAUM, MONEY IN THE LAW NATIONAL AND INTERNATIONAL 543-44 (rev. ed. 1950) [hereinafter MONEY IN THE LAW] (recommending this literal interpretation of the phrase "involve the currency of a member"). But see F. MANN, *supra* note 101, at 391 (arguing that the phrase "which involve the currency of a member" does not refer to the denomination of a specific currency in an exchange contract, but

ever, surrounds the second prong of this definition. British courts, in particular, fail to draw a distinction between necessary and unnecessary involvement.²¹⁹

In *Terruzzi*, the contract between an Italian resident and a British resident called for the use of pounds sterling, not lire.²²⁰ The British Court of Appeal noted that performance of the contract may have required that either one of the parties use lire.²²¹ The House of Lords, in *United City Merchants*, also noted that although Peruvian soles were never named as the currency of use in the contract, their use was indeed necessary for performance.²²² Looking at the entire transaction and the evidence presented, the court found that the use of Peruvian soles was implicitly necessary in effecting the transaction because the entire purpose behind the contract was the fraudulent conversion of Peruvian soles into United States dollars.²²³

An insufficient basis exists for developing a sound legal distinction between *Terruzzi* and *United City Merchants* concerning currency involvement. The use of Italian lire in the *Terruzzi* transaction was as necessary as the use of Peruvian soles in the *United City Merchants* transaction. In the former decision, defendant *Terruzzi* was required to exchange lire for pounds sterling to receive the currency mandated in the transaction.²²⁴ In the latter decision, *Vitro*, the purchasing corporation, was also required to exchange Peruvian soles for United States dollars to effectuate the transaction.²²⁵ Any distinction in reasoning seemingly lies on the perceived intent of the parties engaged in each transaction.²²⁶ Even where the performance of the contract requires the

to the financial area where the transaction has economic effects).

219. *See* *Wilson, Smithett & Cope Ltd. v. Terruzzi*, [1976] 1 Q.B. 683, 719 (C.A.) (stating that courts should not read the phrase "involvement of currency" restrictively, but should link this phrase to the meaning of exchange contracts).

220. *Wilson, Smithett & Cope Ltd. v. Terruzzi*, [1976] 1 Q.B. 683, 719 (C.A.). *See generally* *Weston Banking Corp. v. Turkiye Garanti Bankasi A.S.*, 57 N.Y.2d 315, 684, 442 N.E.2d 1195, 456 N.Y.S.2d 684 (1982) (finding that a promissory note calling for repayment in foreign currency does not violate Turkish currency control regulations because it requires repayment in Swiss francs, not Turkish lire).

221. *Wilson, Smithett & Cope Ltd. v. Terruzzi*, [1976] 1 Q.B. 683, 719 (C.A.).

222. *United City Merchants v. Royal Bank of Canada*, [1983] 1 App. Cas. 168, 182, 190.

223. *Id.*; *see* COURTS II, *supra* note 170, at 333 (noting that if the parties carried out the transaction, the Peruvian buyers would have to repay the debt to their Peruvian bank through the exchange of Peruvian soles for United States dollars).

224. *Wilson, Smithett & Cope Ltd. v. Terruzzi*, [1976] 1 Q.B. 683, 719 (C.A.).

225. *United City Merchants v. Royal Bank of Canada*, [1983] 1 App. Cas. 168, 182.

226. *See id.* (observing that the parties knowingly intended to violate Peruvian exchange control regulations and, therefore, the transactions involved Peruvian soles, the restricted currency); *Wilson, Smithett & Cope Ltd. v. Terruzzi*, [1976] 1 Q.B. 683,

conversion of restricted currency, English courts refuse to admit involvement of that currency if the scheme underlying the transaction is not designed to effect an unlawful exchange. Consequently, whether a currency is involved in an exchange contract depends solely on whether the parties intended the contract to circumvent the relevant exchange control regulations. This standard makes the issue of currency involvement ambiguous and unpredictable.

The courts of all IMF member states do not apply as restrictive an interpretation of involvement. Many courts view the phrase more broadly, indicating that the currency of a member state involves an exchange contract if that contract affects either the exchange resources or balance of payments of the restricting member.²²⁷ Thus, a United States bank seeking to invoke the IMF defense can present this interpretation of currency involvement, if the circumstances do not warrant a successful argument under the literal interpretation of the phrase.

One commentator, favoring a broader interpretation of currency involvement, argues that determining whether the currency of a member country is involved in the transfer of an asset to or from a nonresident nation requires consideration of whether a resident of the member state enters into the exchange contract or deals with assets within the territory of that member.²²⁸ Courts in Germany and France rely on this interpretation in their decisions addressing currency involvement. In the *Clearing Dollars Case*,²²⁹ the plaintiff, a German firm, contracted to sell chemicals to the defendants, Belgian residents, at the price of forty-six United States clearing dollars²³⁰ payable under Belgian-West German Clearing.²³¹ The defendants, failing to acquire the import license required under Belgian exchange control regulations, did not purchase the chemicals.²³² Consequently, the plaintiff sued the defendants seeking damages for breach of contract.²³³

The defendants, raising the IMF defense, stated that if the exchange contract was performed, it would involve the currency of Belgium, Belgian francs.²³⁴ The Hamburg Provincial Court accepted this argument

710-11 (C.A.) (noting that neither party knowingly intended to violate Italian exchange control regulations and, thus, the transaction did not involve lire, the restricted currency).

227. COURTS II, *supra* note 170, at 214.

228. J. GOLD, *THE INTERNATIONAL MONETARY FUND AND PRIVATE BUSINESS TRANSACTIONS* 25 (IMF Pamphlet Series, No. 3, 1965).

229. *Clearing Dollars Case*, 22 I.L.R. 730 (Landgericht, Hamburg 1954).

230. *Id.*

231. *Id.*

232. *Id.*

233. *Id.* at 730.

234. *Id.* at 731.

and held that an exchange contract existed that involved Belgian currency.²³⁵ In so holding, the German court analyzed the residence of the parties, noting that the contract involved residents of Belgium.²³⁶ Furthermore, the court noted that because payment in Belgian francs was required under the clearing arrangements, performance of the contract involved the foreign exchange reserves of Belgium.²³⁷

In *De Boer v. Ducro*,²³⁸ Moojen, a Dutch resident, assigned shares in a French company to a German resident for francs, violating Dutch exchange control regulations.²³⁹ Moojen's widow sought the enforcement of a Dutch judgment finding that the assignment of shares without prior Dutch authorization was void.²⁴⁰ The Paris Court of Appeal enforced the Dutch judgment in France, characterizing the assignment as an exchange contract involving Dutch currency.²⁴¹ The Court stressed that Moojen was a resident of the Netherlands at the time he entered into the agreement,²⁴² and also emphasized that the assignment could affect the exchange resources of the Netherlands.²⁴³ Consequently, the French court took a more liberal approach on the meaning of currency involvement.

In future litigation, United States commercial banks arguing that Eurodollar arrangements are exchange contracts involving United States currency will have to structure their arguments to fit within either a broad or narrow interpretation of currency involvement, depending on the jurisdiction. United States banks can claim that because most Eurodollar contracts name the United States dollar as the medium of repayment,²⁴⁴ the issue of necessity should never arise under a narrow reading of currency involvement. Banks can also argue that Eurodollar contracts involve the exchange resources of the United States. More specifically, United States banks can claim that a

235. *Id.* at 731.

236. *Id.* at 730.

237. COURTS I, *supra* note 212, at 84; see *Clearing Dollars Case*, 22 I.L.R. at 730, 731-32 (noting that payment in Belgium francs under Belgium-West German clearing defeats the purpose of the Belgium exchange control regulations).

238. *De Boer v. Ducro*, 47 I.L.R. 46 (Cour d'appel, Paris, 1961).

239. *Id.* at 52.

240. *Id.* at 48; see COURTS I, *supra* note 212, at 145 (analyzing the *res judicata* effect of the prior Dutch adjudication of the article VIII, section 2(b) issue on the Paris Court of Appeal).

241. *De Boer v. Ducro*, 47 I.L.R. 46, 51 (Cour d'appel, Paris, 1961).

242. *Id.* at 50.

243. *Id.* at 51; see *Baker*, *supra* note 168, at 258 (observing that the assignment as a whole effectively diminished Dutch foreign exchange assets).

244. See *Carreau*, *supra* note 67, at 159 (stating that a Eurodollar deposit refers to a deposit of United States dollars and that the currency of repayment is almost always the currency initially deposited).

Eurodollar arrangement involves assets located in the United States and that a United States resident entered into the Eurodollar contract.

c. United States Asset Freeze as an Exchange Control Regulation

Assuming that a particular Eurodollar arrangement qualifies as an exchange contract involving United States currency, the question then becomes whether the contract violates United States exchange control regulations. This determination requires consideration of whether a politically motivated United States asset freeze is a proper exchange control regulation. The IMF is authorized to determine whether political asset freezes constitute proper exchange control regulations under article VIII, section 2(b), and whether these regulations are consistent with the Articles of Agreement.²⁴⁵

The Executive Directors of the IMF have not promulgated a formal interpretation of exchange control regulations.²⁴⁶ Generally, restrictions on capital movements under article VI, section 3, enactments under articles VIII, section 2(a) and section 3, and monetary measures are included within the definition of exchange control regulations.²⁴⁷ Under article VI, section 3, an IMF member may introduce restrictions on capital movements without the approval of the IMF.²⁴⁸ To impose restrictions on payments or transfers for current international transactions under article VIII, section 2(a), however, a member must seek IMF approval.²⁴⁹ Deciding whether to grant approval requires the IMF to look at the form and technical character rather than the purpose of the regulations.²⁵⁰

The issue remains whether asset freezes are classified as restrictions on capital movements or as restrictions on the making of payments and transfers for current international transactions. The IMF has distinguished between a payment for a current international transaction and payment for a capital movement. Article XXX(d) defines payments for current international transactions, excluding those transactions for pur-

245. See *Callejo v. Bancomer, S.A.*, 764 F.2d 1101, 1120 (5th Cir. 1985) (detailing the IMF approval process that determines whether Mexican exchange controls are consistent with the Articles of Agreement).

246. Edwards, *supra* note 9, at 883.

247. Silard, *Exchange Controls and External Indebtedness: Are the Bretton Woods Concepts Still Workable?*, 1984 AM. SOC'Y INT'L. L. PROC. 240, 241.

248. Agreement, *supra* note 24, art. VII, sec. 3; see GUIDE, *supra* note 150, at 21 (observing that members can restrict capital movements unless such measures hinder payments or transfers for current international transactions).

249. Agreement, *supra* note 24, art. VIII, sec. 2(a).

250. See *Extraterritorial Enforcement*, *supra* note 169, at 353 (asserting that the classification of an exchange control regulation is dependent on its technical character).

poses of transferring capital, to encompass, among other things, all payments due in connection with short-term banking and credit facilities, payments relative to foreign trade, payments due as interest on loans, and payments representing net income from other investments.²⁵¹ Restrictions on capital movements, however, are defined as payments and receipts that are outside the scope of article XXX(d),²⁵² including transfers of funds between countries for investment or speculation.²⁵³

Determining whether an asset freeze, a form of an exchange control regulation, is a restriction on capital movements or a control on current transactions requires an examination of the language of such enactments. The language in prior United States exchange controls prohibited United States residents from paying, withdrawing, exporting, or dealing with the property interest of a nonresident.²⁵⁴ These restrictions defined property interest to include money, checks, drafts, bank deposits, indebtedness, goods, letters of credit, interest, and other periodic payments.²⁵⁵ Some argue, therefore, that this form of an exchange control regulation constitutes a restriction on capital transfers.²⁵⁶ Additionally, some argue that these regulations are restrictions on current transactions under article VIII, section 2(a) because the controls retard payments and transfers in connection with loans, hinder payments due in connection with foreign trade, and affect short-term banking under article XXX(d).²⁵⁷ Therefore, the United States, the country imposing the particular restriction, is only required to seek approval of those enactments relating to current transactions.

Many scholars defining exchange control regulations, however, look to the purpose for imposing controls, rather than their technical form.²⁵⁸ Exchange control regulations include regulations enacted to

251. Agreement, *supra* note 24, art. XXX(d); see COLLABORATION, *supra* note 213, at 395 (remarking that the banking provisions enumerated in article XXX(d) do not cover direct investments).

252. Agreement, *supra* note 24, art. XXX(d).

253. J. HORSEFIELD, *supra* note 150, at 22.

254. See 31 C.F.R. § 550.209 (1987) (describing the prohibitions of transactions involving property where Libya has an interest); see also *id.* § 535.201 (identifying prohibitions of transactions where Iran or its entities have an interest).

255. See *id.* § 550.314 (defining property interest in the Libyan Sanctions Regulations); see also *id.* § 535.311 (identifying all property interests in the Iranian Sanction Regulations).

256. See Pardieu, *The Carter Freeze Order: Specific Problems Relating to the International Monetary Fund*, 9 INT'L BUS. LAW. 97, 99 (1981) (characterizing the Iranian exchange control regulations as restrictions on capital movements).

257. Edwards, *supra* note 9, at 871.

258. See Pardieu, *supra* note 256, at 98 (asserting that a reasonable interpretation of the phrase exchange control regulation analyzes the purposes and effects of the regulations).

protect the financial resources of the country imposing them.²⁵⁹ Under this definition, a regulation adopted for noneconomic reasons does not fall within the definition of a proper exchange control regulation.²⁶⁰ For example, trading with the enemy regulations²⁶¹ and United States exchange controls adopted during World War II²⁶² do not qualify as exchange control regulations within the scope of article VIII, section 2(b).²⁶³

The IMF adopted Decision (52/51), a procedure to regulate restrictions based on political motives in 1952.²⁶⁴ The IMF has jurisdiction over all currency restrictions on current international payments and transfers invoked for national security reasons.²⁶⁵ If restrictions within the scope of article VIII, section 2(a) are imposed for security reasons only, the country imposing these restrictions must seek formal approval from the IMF Directors.²⁶⁶ A member must notify the IMF of the restrictions within thirty days of imposing the restrictions.²⁶⁷ If the IMF does not inform the member of its dissatisfaction with the restrictions within thirty days, the restrictions are presumed valid under the Agreement.²⁶⁸ Ironically, under this procedure, the reasons for imposing the

259. F. MANN, *supra* note 101, at 393.

260. *Id.*

261. Trading with the Enemy Act of 1917, ch. 106, 50 U.S.C. app. § 5(b)(1)(A) (1982).

262. See Exec. Order No. 8,389, 3 C.F.R. § 644, 645 (1940) (promulgating the freezing of Norwegian and Danish assets in the United States, preventing Nazi seizure of such assets); see also Roth, *Statutory Basis for the Iranian Asset Freeze*, 3 CORP. L. REV. 165, 168 (1980) (stating that assets were frozen under the Trading with the Enemy Act for the first time in 1940).

263. MONEY IN THE LAW, *supra* note 218, at 455-57.

264. SELECTED DECISIONS, *supra* note 27, at 253. This decision dates back to 1950 when the United States imposed restrictions on China and Korea. COURTS II, *supra* note 170, at 366. President Truman declared a national emergency under the Trading with the Enemy Act when China entered the Korean War in 1950. TREASURY PAMPHLET, *supra* note 1, at 7. Subsequently, the Treasury Department promulgated the Foreign Asset Control Regulations that apply to North Korea, Cambodia, and South Vietnam. *Id.* China and the United States reached a settlement on May 7, 1979, releasing \$80.5 million in frozen Chinese assets. *Id.*

265. SELECTED DECISIONS, *supra* note 27, at 253.

266. *Id.*

267. *Id.*

268. *Id.* at 253-54. During the Iranian asset freeze, the United States executive directors reported the Iranian restrictions to the Executive Director of the IMF and invoked Decision 144. COURTS II, *supra* note 170, at 361. The freeze occurred on November 14, 1979, and the United States circulated its memorandum to the IMF Executive Board on November 29, 1979. *Id.* The IMF did not object within the 30 day limit. Edwards, *supra* note 9, at 875. On April 7, and 17, 1980, President Carter amended the Iranian regulations. *Id.* at 872. The United States notified the Board of these amendments on April 28, 1980, and the Board took no action within the 30 day limit. *Id.* at 875-76.

restrictions are irrelevant.²⁶⁹

Unfortunately, the IMF approval process has one major flaw. United States banks relying on the IMF defense in potential litigation involving national exchange controls will never know whether the IMF has approved the controls prior to any litigation between the bank and its depositor.²⁷⁰ The IMF does not immediately issue press releases to banks informing the banks of its decision to approve exchange controls on current transactions adopted for economic or security reasons.²⁷¹ In addition, it does not publicly announce its approval of exchange control regulations in either its Annual Report or in its Annual Report on Exchange Arrangements and Exchange Restrictions.²⁷² Nevertheless, following the commencement of litigation between a bank and its depositor, the IMF will respond to inquiries from courts or parties on whether the IMF approved particular exchange controls.²⁷³ Consequently, although banks can examine precedent to determine whether the IMF will treat a Eurodollar as an exchange contract, the banks cannot obtain information detailing the IMF's approval of an exchange control prior to litigation.

The IMF, therefore, should establish procedures that open the approval process to the financial communities of member states, provide clear guidelines of the approval process to interested private parties such as banks, and maintain the degree of confidentiality necessary to protect the interests of the IMF. These procedures would require a bank to analyze its nation's exchange controls following their enactment and would mandate that the bank then determine how these controls affect its interests. Following a timely review, if the bank finds that these exchange controls hinder withdrawals, transfers, or payments to its depositor and this depositor maintains enormous accounts with the bank, then the bank could prepare a special request to the IMF to obtain information on whether the IMF approved the exchange control restrictions. The IMF could require the submission of this special request for information relating to the approval of exchange control regulations within a certain fixed period following the enactment of the regulations. The IMF, while reviewing each bank's request on a case-by-case basis, would either reject the request or send the requested infor-

269. SELECTED DECISIONS, *supra* note 27, at 253.

270. Zamora, *Exchange Controls and External Indebtedness: Are the Bretton Woods Concepts Still Workable?*, 1984 AM. SOC'Y INT'L L. PROC. 240, 249.

271. *Id.*

272. RESTATEMENT OF THE FOREIGN RELATIONS LAW OF THE UNITED STATES (REVISED), § 822 comment C (Tent. Draft No. 6, 1985).

273. *Id.*

mation. Additionally, the IMF could establish helpful guidelines for future applicants detailing the proper procedures for making these requests. Therefore, banks informed of an IMF decision to approve asset freezes imposed for security reasons can, prior to any potential litigation, structure an IMF defense more precisely. Moreover, these procedures will facilitate greater cooperation between private parties and the IMF.

If a Eurodollar transaction is an exchange contract involving United States currency, it cannot contradict United States exchange control regulations. In identifying proper exchange control regulations, some jurisdictions look to the technical language of the exchange restrictions, whereas other jurisdictions look to the purposes behind the enactment of the exchange controls. Consequently, it is more difficult to classify an asset freeze under the latter definition than the former.

d. The United States Asset Freeze as Exchange Control Regulations Consistent with the IMF Agreement

Although the IMF may recognize a particular United States asset freeze as an exchange control regulation, it may still refuse to concede that the freeze is consistent with the purpose and the spirit of the IMF Agreement. If the IMF has approved a member's restrictions, however, the regulations are usually consistent with the Agreement.²⁷⁴ Since 1949, the IMF has argued that it should advise all members on whether their exchange control regulations were imposed consistently with the Agreement.²⁷⁵ Various national courts, however, disagree on whether express approval from the IMF is required.

United States courts have held that advice from the IMF is determinative of the consistency of exchange control regulations.²⁷⁶ Similarly, English courts have deferred to evidence of IMF approval relating to the consistency of exchange control regulations with the agreement.²⁷⁷ Belgian courts, however, have required a stricter proof of specific IMF approval of exchange control regulations.²⁷⁸ German courts have noted

274. COLLABORATION, *supra* note 213, at 483.

275. SELECTED DECISIONS, *supra* note 27, at 252.

276. *Southwestern Shipping Corp. v. National City Bank of New York*, 173 N.Y.S.2d 509, 523, 11 Misc.2d 397, 410 (1958). The IMF advised the New York Supreme Court that Italian exchange control regulations were consistent with the Agreement. *Id.*

277. *Wilson, Smithett & Cope Ltd. v. Terruzzi*, [1976] 1 Q.B. 683, 719 (C.A.). The British court also indicated that in the future, it would listen to expert evidence on the effect of the exchange control regulations. *Id.*

278. *Emek v. Bossers & Mouthaan*, 22 I.L.R. 722, 724 (Belgium Commercial Tribunal of Courtrai 1953). *Contra* COURTS I, *supra* note 212, at 82 (criticizing the

that exchange control restrictions can be consistent with the Articles of Agreement without express approval from the IMF.²⁷⁹ Under the German approach, if the IMF approves the general nature of the regulations or the customary state practice mandates the validity of such exchange controls, then the exchange control regulations are consistent with the IMF Agreement.²⁸⁰

Finally, if the IMF approves an asset freeze as a proper exchange control regulation, it may also determine that such regulations are consistent with the IMF Agreement. Some jurisdictions require the litigating parties to obtain advice from the IMF on whether the IMF has approved particular exchange control regulations, whereas other jurisdictions may not require this information from the IMF.

III. IMPLICATIONS OF THE DECISION IN *LIBYAN ARAB FOREIGN BANK V. BANKERS TRUST CO.*

The underlying reasons behind the decision of the English court in *Libyan Arab Foreign Bank v. Bankers Trust* are two-fold. The British Court's acceptance of the United States Eurodollar defense could have produced a major disruption in the Eurodollar market. Fearing the political risks involved in holding Eurodollar deposits, potential Eurodollar depositors would not invest in such a market²⁸¹ and those depositors already holding Eurodollar deposits would withdraw their funds, placing them in alternative financial markets.²⁸² These actions ultimately could have led to the crash of the Eurodollar market; the United Kingdom therefore would have lost its standing as the premier holder of Eurodollar deposits. United States banks may then become outcasts in the international financial community. Furthermore, the United States dollar could lose its status as a premier reserve currency.²⁸³

The decision of the court in *Libyan Arab Foreign Bank v. Bankers Trust* also showed that the United States cannot act unilaterally in in-

Belgium court for requiring specific proof of IMF approval).

279. Clearing Dollars Case, 22 I.L.R. 730, 731 (Landgericht, Hamburg 1954).

280. *Id.*

281. See Financial Times, Sept. 24, 1987, at 8, col. 1 (understanding that a potential Eurodollar depositor has relevant concerns regarding the security of the Eurodollar market); Carswell, *Economic Sanctions and the Iran Experience*, 60 FOREIGN AFF. 247, 262-63 (1981-82) (addressing the concerns of United States bankers during the Iranian asset freeze that OPEC countries would reduce their holding of assets in the Eurodollar market).

282. See Lissakers, *Money and Manipulation*, 44 FOREIGN POL'Y 107, 120-21 (noting the concerns of Treasury officials and bankers, during the Iranian asset freeze, that investors, especially from the Middle East, would look toward European financial institutions as an alternative).

283. *Id.* at 122.

voking asset freezes without first obtaining the assistance of other countries. The United States should seek the cooperation of all countries that are holders of Eurodollar accounts before freezing accounts.²⁸⁴ Countries, holding these accounts, may agree to fight international terrorism through allowing the United States to freeze Eurodollar accounts temporarily until that particular country involved in terrorism stops these violent actions.²⁸⁵ The United States, however, must realize that some countries are opposed to any type of economic sanctions because the costs of such an action to their own economies are high.²⁸⁶ Therefore, the United States should encourage mutual agreements with other nations to collectively combat terrorism through asset freezes.

CONCLUSION

In *Libyan Arab Foreign Bank v. Bankers Trust Co.*, Bankers Trust Company had to honor the Libyan demands for repayment of the Eurodollar account. The repayment was not illegal under English law, the proper substantive law governing the Eurodollar deposit contract. Furthermore, the repayment did not necessitate actions in an illegal forum. This decision acted as a deterrent for countries wishing to invoke asset freezes of Eurodollar accounts in the future. Even though the mechanism of repayment ordinarily occurs in the United States through CHIPS, countries will rely on this decision and require alternative methods of repayment to the depositor. Finally, if the United States invokes an asset freeze in the future, it should raise the IMF defense if the country where the Eurodollar account is located supports a broad interpretation of article VIII, section 2(b).

POSTSCRIPT

In *Libyan Arab Foreign Bank v. Bankers Trust Co.*, Bankers Trust Company opted to forego an appeal to the British Court of Appeal.²⁸⁷

284. *Id.* at 125; cf. Carswell, *supra* note 281, at 264-65 (noting the minimal effects of a United States unilateral asset freeze without obtaining multilateral support).

285. See Financial Times, Sept. 25, 1987, at 6, col. 2 (raising the possibility of combatting terrorism through the assistance of all countries in the support of asset freezes).

286. Wash. Post, Jan. 9, 1986, at A15, col. 1; see Wall St. J., Jan. 9, 1986, at 25, col. 1 (describing the resistance of Asian, Moslem, and Communist countries to the use of economic sanctions as a deterrent measure against terrorism). After President Reagan froze Libyan assets in overseas branches of United States banks, he recognized the need for the multilateral cooperation of the European Community in his fight against international terrorism. President Reagan's Interview with European Journalists of January 10, 1986, 22 WEEKLY COMP. PRES. DOC. 41 (Jan. 20, 1986).

287. Wall St. J., Oct. 13, 1987, at 31, col. 1.

In addition, on October 10, 1987, the United States Treasury Department issued a license to Bankers Trust Company, permitting it to repay \$320.1 million²⁸⁸ to the LAFB.²⁸⁹ Because the Treasury Department issued a special license to Bankers Trust Company, the bank did not violate United States law under the Libyan Sanctions Regulations in making the repayment.²⁹⁰ The Treasury Department issued the license to Bankers Trust without a public explanation.²⁹¹

288. *See id.* (noting that the \$292 million sum represented the deposits owed to the LAFB and the remainder represented interest owed to the plaintiff).

289. *Id.*

290. 31 C.F.R. § 550.209 (1987).

291. Wall St. J., Oct. 13, 1987, at 31, col. 1.