

## FTR Now

# Sovereign Immunity and The “Commercial Activity” Exception

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Late last year, the Supreme Court of Canada ruled that Iraq could not rely on state immunity to bar the enforcement of an English judgment ordering Iraq to pay CAD\$84 million to the Kuwait Airways Corporation. In *Kuwait Airways Corp. v. Iraq* [1], the Court determined that within the context of the dispute, Iraq was not immune from the jurisdiction of Canadian courts as the activity in question was commercial in nature.

Although this decision does not explicitly deal with employment law, it could have an impact for Embassy and High Commission employers as it relates to sovereign immunity and the “commercial activity” exception carved out by the *State Immunity Act*. This *FTR Now* considers the decision and its implications for those employers.

## BACKGROUND: STATE IMMUNITY AND THE “COMMERCIAL ACTIVITY” EXCEPTION

Foreign state immunity in Canada is governed by the *State Immunity Act*. Under the *Act*, a foreign state is immune from the jurisdiction of any court in Canada unless one of the enumerated exceptions applies. Notably, these exceptions include cases where the proceedings relate to any “commercial activity” of the foreign state.

In cases involving employment contracts, decision makers have sought to distinguish between aspects of the employment relationship that are “commercial” in nature and those that are “sovereign”, with the result that there is rarely a clear demarcation. While the Supreme Court of Canada has stated that bare employment contracts are primarily commercial in nature, cases have been fact-driven and courts have been reluctant to apply the commercial activity exception to state immunity for wrongful dismissal actions, instead finding that they would be required to pry too deeply into the inner workings of the sovereign state to properly resolve these disputes.

The leading case on point is *United States of America v. Public Service Alliance of Canada et al.* [2] (hereinafter *Re Canada Labour Code*) in which the Supreme Court of Canada decided that the United States was entitled to state immunity when a union applied for certification of the Canadian civilian trade people working for it on the United States naval base established in Newfoundland, Canada. In the judgment, the Supreme Court of Canada ruled that when characterizing state activity as “sovereign” or “commercial”, it is essential to view the activity in its entire context. Both the nature of the activity and its purpose may be relevant.

Subsequent cases have demonstrated that the commercial activity exception is difficult to apply and is highly fact driven. In *Butcher v. Saint Lucia* [3], the plaintiff claimed that the defendant breached the terms of the employment contract. The Court concluded that although the claims related in part to the commercial aspect of an employment contract, the more significant impact of the claim related to issues impacting state sovereignty and accordingly the action for breach of contract was stayed and the Government of Saint Lucia was entitled to sovereign immunity.

In another interesting case, *Greco v. Holy See (State of the Vatican City)* [4], a United States citizen employed as a member of the administrative staff at the Apostolic Nunciature to Canada brought an action against the Vatican for breach of contract. The plaintiff made various claims including claims for lost wages and termination without cause prior to the end of a fixed-term contract. The Superior Court found the contract of employment had both commercial and sovereign aspects. It held that the enforcement of specific contract terms such as unpaid wages fell within the commercial activity exception to state immunity and therefore that portion of the claim was not stayed. However, the Superior Court found that the claim for

wrongful dismissal had a substantial impact on the sovereign aspect of the employment contract and the proceedings would have a significant impact of the sovereign right of the defendant state to control its own workforce. Accordingly the wrongful dismissal portion of the claim was stayed.

## KUWAIT AIRWAYS CORP. V. IRAQ

In *Kuwait Airways Corp. v. Iraq*, the Supreme Court of Canada confirmed the contextual analysis set out in *Re Canada Labour Code*. The plaintiff, a Kuwaiti airline, had obtained a judgment in England against Iraq's national airline, for damages suffered as a result of the Iraqi airline's appropriation of aircraft and equipment following Iraq's 1990 invasion of Kuwait. The English court also found that the Iraqi government had controlled, funded, and supervised its airline's legal defence, and accordingly held the Republic of Iraq liable for the Kuwaiti airline's litigation costs, in the amount of approximately CAD\$84 million.

The Kuwaiti airline discovered immovable property owned by Iraq in Quebec and also some undelivered airplanes Iraq was buying from Bombardier Aerospace. The Kuwaiti airline therefore sought to enforce its English judgment for costs against assets owned by the Republic of Iraq in Quebec. Iraq argued that the judgment could not be enforced anywhere in Canada, as it was entitled to immunity pursuant to the *State Immunity Act*.

Overtaking the lower court decisions, the Supreme Court of Canada found that the English litigation did not concern the initial sovereign act of seizing the aircraft. Rather, it concerned acts performed by Iraq in the course of the proceedings in the English courts. The subject of the litigation was the commercial act of the retention and use of the aircraft by the Iraqi airline. As a result, Iraq could not rely on state immunity to bar the enforcement of the English judgment.

In its reasons, the Supreme Court of Canada reinforced the principle that it is not enough to determine whether the acts at issue were authorized or desired by the state or whether they were performed to preserve certain public interests of that state. The question of whether the commercial activity exception applies to state immunity is determined by first reviewing the nature of the acts in issue in the action in their full context, which includes the purpose of the acts.

## CONCLUSION

In essence, the Supreme Court of Canada has preserved the general approach to dealing with questions of sovereign immunity and the application of the commercial exception to employment contexts. The *Kuwait Airways* case dealt with truly commercial issues, rather than employment issues. Still, it remains to be seen whether lower courts will apply the "commercial activity" exception to state immunity more broadly, including in the employment context, in light of the Court's conclusions. Embassies and High Commissions which are employers of locally engaged staff in Canada may wish to review their employment contracts and policies to ensure that their interests – particularly whether or not they wish their employment relations with locally engaged staff to be subject to local laws – remain properly protected following this legal development.

If you have any questions about this decision, please contact [George Vuicic](#) at 613.369.2103, [Siobhan O'Brien](#) at 613.369.8411, or your regular [Hicks Morley lawyer](#).

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[1] 2010 SCC 40

[2] (1992), 91 D.L.R. (4th) 449

[3] [1998] O.J. No. 2026, aff'd by the Supreme Court of Canada [1999] O.J. S.C.C.A. No. 322

[4] [1999], O.J. No. 2467, rev'd in part in [2000] O.J. No. 5293



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