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Sovereign Wealth Funds: Evolving Perceptions and Strategies



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General levels of interest in the activities and motivations of ''sovereign wealth funds'' (''SWFs'') have waxed and waned over the last several years, with interest being more acute in the years before the recent financial crisis as SWFs became more numerous, larger and more active, including in the United States and Europe, and increasing again more recently as several transactions and situations involving SWFs have become newsworthy. This article discusses the nature and activities of SWFs, certain distinctions between SWFs and other investors, certain relevant U.S. tax and legal matters, and the evolving strategies and behaviors of SWFs.

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What Are SWFs?

Despite the amount of attention that sovereign wealth funds have garnered over the last few years, there is no universal definition of a ''SWF''. The term has been used to cover a spectrum of government investment vehicles from central banks and monetary authorities to government-owned enterprises that invest in specific economic sectors. Several organizations and commentators have offered somewhat different definitions that can affect whether certain institutions would be considered SWFs.[1] These definitions generally tend to focus on how the institutions are funded, the type of assets they hold or how their assets are managed.[2]

For instance, the International Working Group of Sovereign Wealth Funds (the ''IWG'') has defined SWFs as special purpose investment funds or arrangements that are established and owned by governments for macroeconomic purposes to hold, manage or administer assets to achieve financial objectives and to employ various investment strategies, including invest-

[1] Preqin Ltd., *The 2012 Preqin Sovereign Wealth Fund Review* (2012) (the ''Preqin Review'').

[2] Simone Mezzacappo, *The so-called ''Sovereign Wealth Funds'': regulatory issues, financial stability and prudential supervision*, Economic Papers 378 (April 2009).

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ment in foreign financial assets.[3] The IWG notes that SWFs are commonly established out of balance of payments surpluses, official foreign currency operations, the proceeds of privatizations, fiscal surpluses and/or receipts resulting from commodity exports. Commodity-funded SWFs constitute 91 percent of SWFs by number and over 99 percent of the aggregate assets under management of all SWFs, with revenues from the export of hydrocarbons alone accounting for about 52.6 percent of SWF assets under management.[4]

Some researchers have developed more precise definitions. For example, Monitor Company Group defines a SWF as an investment vehicle that (i) is owned directly by a sovereign government, (ii) is managed independently of other state financial institutions, (iii) does not predominately have explicit pension obligations, (iv) invests in a diverse set of financial asset classes in pursuit of commercial returns and (v) has made a significant proportion of its publicly reported investments internationally.[5] Monitor Company Group has made exceptions to the first criterion for funds based in the United Arab Emirates because each emirate, though not technically a sovereign government, has decision rights comparable to those of sovereign authorities, while excluding funds such as those in Alaska and Alberta because it does not believe that sub-national governments in North America possess those decision rights.[6]

For purposes of simplicity, this article generally uses the term ''SWF'' to encompass the broader spectrum of entities.

Investments of SWFs.

Historically, SWFs' investment strategies have typically focused on ''developed'' Western countries. Recently, SWFs have invested more in emerging markets, particularly in the Asia Pacific region; in the second half of 2010, more than half of publicly reported direct investments by SWFs, accounting for 79 percent of total investment, occurred in emerging markets. In addition, Brazil, Russia and India have been the focus of more investment by SWFs than ever before, with Singapore's funds investing particularly heavily in India. Even markets in sub-Saharan Africa that have historically struggled to attract foreign investment have more recently been the locus of substantial SWF activity.[7]

This trend shows no signs of abating, in part because the Euro-zone debt crisis may have deterred SWFs from investing in bonds originating from countries in that region.[8] Another reason for this increased geographic diversity may be the concentration in Asia, the Middle East and North Africa of 54 percent of all SWFs, accounting for 77 percent of total assets under management.[9] As these funds have grown and new ones have emerged in these regions, local investments have constituted increasing portions of their portfolios, resulting in increased total investment in these markets.

Investment objectives and strategies vary significantly among SWFs, although two identifiable strategic approaches tend to be the most common.[10]

First is the ''portfolio management'' approach, whereby a SWF diversifies investments based on global criteria aimed at outperforming benchmark indexes but does not overtly specialize in any one sector or become involved in the management of the companies in which it invests.[11] Funds that have traditionally taken this approach include the Abu Dhabi Investment Authority (''ADIA''), the Government Pension Fund of Norway and the Government of Singapore Investment Corporation (''GIC'').[12] For instance, GIC states that its mission is to preserve and enhance the international purchasing power of the reserves placed under its management with the aim of achieving good long-term returns above global inflation over the investment time horizon of 20 years.[13]

In contrast, SWFs that take the ''investment fund'' approach apply a rigorous methodology to invest in sectors that are strategically important to their home countries' development.[14] These SWFs tend to make larger and more concentrated investments and to be more actively involved in the management of the companies in which they invest. Temasek Holdings (''Temasek'') in Singapore and the Qatar Investment Authority fall into this second category of SWFs, although Temasek generally refrains from involvement in the commercial or operational decisions of the companies in which it invests and does not, as a general matter, seek to be represented on the boards of its investees.[15]

However, more recently established SWFs sometimes have different approaches and goals – for example, Fonds Stratégique d'Investissement in France, initiated in 2008 and with $25 billion of assets, has as its stated goal increasing the competitiveness of French

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[3] International Working Group of Sovereign Wealth Funds, *Sovereign Wealth Funds: Generally Accepted Principles and Practices* (October 2008) (the ''Santiago Principles'') (available at: *http://www.iwg-swf.org/pubs/eng/santiagoprinciples.pdf*).

[4] The Preqin Review.

[5] Monitor Company Group, L.P., *Braving the New World: Sovereign Wealth Fund Investment in the Uncertain Times of 2010* (June 2011) (the ''2011 Monitor Report'') (available at: *http://www.monitor.com/Portals/0/MonitorContent/imported/MonitorUnitedStates/Articles/PDFs/BTNW_Final.pdf*).

[6] *Id.*

[7] The 2011 Monitor Report.

[8] The Preqin Review.

[9] *Id.*

[10] Alan Demarolle, *Report to the Government of France on Sovereign Wealth Funds* (November 11, 2008) (''The Government of France Report'') (available at: *http://www.paris-europlace.net/files/rapport_demarolle_en.pdf*).

[11] *Id.*

[12] *Id.*

[13] GIC's Report on the Management of the Government's Portfolio for the Year 2011/12 (available at: *http://www.gic.com.sg/data/pdf/GIC_Report_2012.pdf*).

[14] The Government of France Report.

[15] The Temasek Review; Temasek Charter 2009 (available at: *http://www.temasek.com.sg/Documents/userfiles/files/Charter_2009.pdf*).

businesses through taking minority stakes in small and medium size French companies.[16] In addition to assisting the development of their countries' economies generally, some SWFs are established to help a specific industry. For instance, part of the mission of Korea Investment Corporation, established in 2005, is to contribute to advancing Korea's financial industry and promoting Korea's role in the global financial markets.[17]

As SWFs become larger and more numerous, they are also investing in an increasingly broad range of assets. Public equities holdings constitute a significant portion of most SWFs' portfolios, with 84 percent of SWFs known to be investing in this asset class. Fixed income investments have traditionally been important components as well, with 82 percent of SWFs investing in these assets. However, these asset classes may begin to account for a decreasing share of SWFs' assets under management as many funds seek diversification and higher returns from other investments.[18]

SWFs have been increasingly directing funds toward assets other than stocks, bonds and cash. In 2011, the proportion of SWFs investing in private equity, real estate and infrastructure rose significantly – around 57 percent of SWFs now invest in private equity funds, and SWFs have increasingly begun to invest in hedge funds.[19] As of the end of the first quarter of 2012, the number of SWFs investing in alternative investments had increased further, though the proportion of SWFs investing in these assets had actually decreased slightly, probably because of the launch of several new funds that did not or do not yet have these programs. This overall increase has come at a time when other types of investors have begun to take a cautious approach toward alternative investments, so that SWFs are an increasingly important source of capital for managers of these types of investments.[20]

Distinctions From Other Investors

A number of characteristics differentiate SWFs from other types of investors or acquirors. First is their size. While previous predictions of the growth in SWFs have fallen short – according to a US Government Accountability Office 2008 report, SWFs were estimated to have aggregate assets of $6 trillion by 2012, and were forecasted to have up to $13.4 trillion by 2017 – total assets under management of SWFs are still very significant.[21] Aggregate SWF assets are valued at over $4.6 trillion, an increase of 15% in the last year, with the three largest SWFs estimated to have over $1.5 trillion and approximately 60 percent of SWFs managing between $1 billion and $50 billion in assets.[22] In contrast, the total assets under management of private equity firms, which are far more numerous than SWFs, are estimated to be approximately $2 trillion, with only the very largest firms approaching $50 billion.[23] Hedge funds, which are similarly more abundant than SWFs, have assets under management of approximately $2.6 trillion.[24]

Another important distinction between SWFs and other types of investors is their ability to act quickly. Whereas private equity firms, hedge funds and many other types of investors often have internal governance, funding and other processes that prevent them from acting quickly, SWFs generally have significant amounts of autonomy and immediate access to large amounts of capital, which, at least during the recent financial crisis, enabled them to be a crucial lifeline for many prominent commercial and investment banks (including Citigroup (ADIA), UBS (GIC), Morgan Stanley (China Investment Corporation (''CIC'')), Credit Suisse (Qatar Holding LLC (''Qatar Holding'')) and Merrill Lynch (Temasek, Kuwait Investment Authority (''KIA'') and Korea Investment Corporation)).

In addition, SWFs are generally subject to fewer public reporting obligations, although there has been a trend towards greater transparency in the last five years, with many SWFs now issuing annual reports, disclosing financial information and, in some instances, having publicly issued indebtedness.

On the less positive side, SWFs were, at least several years ago, subject to more scrutiny than other investors because of concerns regarding their motivations and, in particular, that they might use their influence on their portfolio companies, whether explicit or implicit, to secure technology or gain access to vital domestic resources to improve the position of their ''home country'' companies. However, these concerns have been less apparent more recently, perhaps because of the initiatives, both bilateral and multilateral, that have been taken by SWFs towards increased transparency, because of the important role SWFs played in providing critical financial support to financial institutions during the financial crisis and, most importantly, because the fears regarding the motivations of SWFs do not appear to have been realized.

SWFs are also eligible for favorable U.S. tax treatment in respect of their investments in U.S. entities. Subject to certain exceptions, Section 892 of the U.S. Internal Revenue Code generally exempts from U.S. federal income taxation certain types of passive income earned by an integral part of a foreign government. SWFs, so long as they are wholly owned and controlled by a foreign government (referred to as ''controlled entities''), are also eligible for this exemption so long as they satisfy certain requirements.

Where applicable, the Section 892 exemption generally applies to dividends (other than certain dividends from real estate invest trusts), interest, gain from the disposition of stocks, and income from investments in financial instruments held in the execution of governmental financial or monetary policy. No exemption is

[16] Matt Miller, *Sovereign wealth funds return*, The Deal Magazine (May 4, 2012).

[17] Korea Investment Corporation's Creating Wealth for the Future Generations, Annual Report 2011.

[18] The Preqin Review.

[19] *Id.*

[20] *Id.*

[21] United States Government Accountability Report to the Committee on Banking, Housing, and Urban Affairs, U.S. Senate, ''Sovereign Wealth Funds'' (September 2008).

[22] The Preqin Review.

[23] Private Equity International, *The PEI 300* (2011) (available at: *http://www.peimedia.com/resources/PEI%20300/PEI300%20-%20Top%2050.pdf*); TheCityUK, *Private Equity* (July 2012) (available at: *http://www.thecityuk.com/assets/Uploads/Private-Equity-2.pdf*).

[24] Peter Laurelli, *New Allocations to Hedge Funds Far Outpaced Redemptions in August*, eVestment|HFN (September 28, 2012) (available at: *https://www.hedgefund.net/dailyemailreports/ResearchRelease_AssetFlows_AUG12.pdf*).

available, however, for income that is derived by a ''controlled commercial entity'' of a foreign government (or gain from the disposition of an interest in a controlled commercial entity) or earned from the conduct of a ''commercial activity''.

A controlled commercial entity is defined as any entity engaged in any ''commercial activities'' if the foreign government either (i) holds 50 percent or more of the interests in the entity (by vote or value) or (ii) holds any interest in the entity which provides the foreign government with ''effective practical control'' of the entity. Commercial activities, in turn, generally include all activities, whether conducted within or outside the U.S., that are ordinarily conducted with a view towards the current or future production of income or gain (other than certain passive investment activities). Commercial activities, however minor, can disqualify all other investments by a controlled entity from exemption under Section 892. In contrast, a foreign government or an integral part will continue to benefit from the Section 892 exemption with respect to its investment activities even if it itself engages in commercial activities.

Under recently proposed regulations, the conduct of an ''inadvertent'' commercial activity will not cause a controlled entity to be considered a controlled commercial entity so long as the commercial activity is ''cured'' within 120 days of discovery and the failure was reasonable.[25] A safe harbor is provided under which failure will be considered reasonable as long as the commercial activity involved no more than five percent of the entity's assets and generated no more than five percent of its gross income, but only if the entity had adequate written policies and operational procedures to monitor the entity's worldwide activities, and management level employees made reasonable efforts to establish, follow and enforce such policies and procedures. Furthermore, although partners in a partnership (other than a publicly traded partnership) engaged in commercial activities are generally treated as engaged in the commercial activities of the partnership, under the proposed regulations no commercial activities are attributed from a non-controlled partnership to a ''limited partner.'' Although the proposed regulations are not effective until published, taxpayers are permitted to rely on them until the final regulations are issued.

U.S. Legal Issues – Applicability to SWFs

The U.S. has a general policy of openness to foreign investment, and its federal laws do not specifically address investments by SWFs.[26] Nonetheless, these laws do restrict foreign investment in certain assets and impose certain other requirements that require the attention and compliance of any potential foreign investor, including SWFs.[27]

1. CFIUS Review

The Committee on Foreign Investment in the United States (''CFIUS'') is an interagency panel chaired by the Secretary of the Treasury, with a mandate to review for potential national security implications any transaction that would result in ''foreign control'' of a U.S. company. Following this review, the President of the United States is authorized to suspend or prohibit certain transactions which would result in foreign control of any business engaged in interstate commerce in the U.S. and would threaten to impair U.S. national security.

The federal law governing CFIUS is Section 721 of the Defense Production Act of 1950, as amended by the Foreign Investment and National Security Act of 2007 (''FINSA'').

Following the controversies arising from the China National Offshore Oil Corporation (or ''CNOOC'')/Unocal transaction in 2005, and the Dubai Ports World/Peninsular and Oriental Steam Navigation Company transaction in 2006, including vocal criticism of CFIUS because of its failure to block either transaction, the U.S. Congress passed FINSA in 2007.[28] The new law includes the protection of critical infrastructure as a factor for CFIUS to consider in its national security reviews and also requires that CFIUS provide reports to Congress regarding each transaction that it reviews.[29]

Filing with CFIUS is voluntary, but it is the only way to obtain ''safe harbor'' from the President's otherwise indefinite power to block or unwind any cross-border transaction that could threaten U.S. national security. A factual predicate for any action by CFIUS to block or unwind a transaction is that the transaction result in ''foreign control''. No ''control'' exists where securities are held ''solely for the purpose of passive investment'' and the acquiror ''has no intention of determining or directing the basic business decisions of the issuer''. Board seats and the ability to make key corporate decisions (including through minority rights provisions) are considered factors that could establish control. Passive investments falling below 10 percent and with no indicia of control are not generally subject to CFIUS review, but there is no automatic exclusion for such investments, as the investor must remain passive and maintain that sole intent regardless of its ownership interest.[30] In addition, 50/50 joint ventures involving a foreign person will be deemed to involve foreign control of a U.S. business if that business is contributed to or otherwise a part of that joint venture.[31]

The CFIUS review process begins with an initial notice filed jointly by all of the parties to the transaction. In addition, the parties are encouraged to submit a draft ''pre-filing'' with CFIUS in advance of the formal notice. CFIUS's review is confidential, and there can be no public disclosure of information received by it. The notice must include personal identification information for all officers and directors of the foreign company and its parents. Most initial reviews are concluded within 30 days.[32]

However, CFIUS undertakes an additional 45-day review where it determines that (i) the transaction could threaten national security and the threat has not been mitigated, (ii) the transaction would result in foreign

[25] Notice of Proposed Rulemaking, REG-146537-06, 76 F.R. 68119 (Nov. 3, 2011).

[26] United States Government Accountability Office, *Sovereign Wealth Funds: Laws Limiting Foreign Investment Affect Certain U.S. Assets and Agencies Have Various Enforcement Processes*, Report to the Committee on Banking, Housing, and Urban Affairs, U.S. Senate (May 2009) (the ''2009 GAO Report'').

[27] *Id.*

[28] The 2009 GAO Report.

[29] *Id.*

[30] 50 U.S.C. App. § 2170; 31 C.F.R. §§ 800.301302; 73 Fed. Reg. 74567.

[31] *Id.*

[32] *Id.*

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control of a U.S. business by a foreign government or foreign government-controlled entity (e.g., any control transaction involving a SWF) or (iii) the transaction would result in foreign control of U.S. ''critical infrastructure'' and could impair national security without mitigation. If CFIUS cannot conclude following its additional 45-day review that the transaction does not pose a threat to U.S. national security, it must make a recommendation to the President, who has 15 days to permit, block, or unwind the transaction, as applicable.[33]

The President has blocked a foreign transaction in this manner only twice, as transactions that CFIUS finds to pose a threat to national security are usually withdrawn before a recommendation is made to the President.[34] The first time was in 1990, when President George H.W. Bush prevented the acquisition of MAMCO Manufacturing, a Washington-based manufacturer of motors and generators, by China National Aero-Technology Import & Export Corp.[35] The second time also involved Chinese investors, when in September 2012, President Barack Obama approved CFIUS's recommendation to order Ralls Corp., a Delaware company owned by two executives of China's Sany Group, to divest their interest in certain wind farm projects in Oregon.[36] Although Ralls Corp. and Sany Group are not SWFs, some commentators believe that the unusual decision of the President to block a foreign transaction in this manner reflects mounting tension with China, which could extend to future proposed investments in the U.S. by Chinese SWFs.

2. HSR Act

The Hart-Scott-Rodino Antitrust Improvements Act of 1976, 15 U.S.C. § 18(a) (the ''HSR Act''), requires that certain proposed acquisitions of voting securities, noncorporate interests or assets be reported to the Federal Trade Commission (the ''FTC'') and the Department of Justice (the ''DOJ'') prior to consummation. Whether a particular acquisition is subject to these requirements depends in part upon the value of the acquisition and the size of the parties, as measured by their sales and assets; the precise amounts are adjusted annually. The parties to the transaction must then wait for a specified period, usually 30 days, before they may complete the transaction. If either the FTC or the DOJ determines that further inquiry is necessary, it may request additional information or documents from the parties. Such a request extends the waiting period, usually by another 30 days that only begins to run following substantial compliance by both parties to the request, so that the agency can complete its review. If the agency finds that the proposed transaction could violate U.S. antitrust laws, it may then seek an injunction in federal court to prevent the consummation of the transaction.[37]

A threshold question for applicability of the HSR Act to a particular transaction is whether each party is considered an ''entity'' under the statute. The term ''entity'' is defined broadly to include natural persons, corporations and many other organizations, but it does not include ''any foreign state, foreign government, or agency thereof (other than a corporation or unincorporated entity engaged in commerce)''.[38]

The FTC Premerger Notification Office (the ''PNO'') has affirmed in informal interpretations of the HSR Act that a government ''agency'' is not subject to the statute. In those interpretations, the PNO has looked to the entity's enabling legislation to determine whether it was created as an ''agency'' of the government or a corporation engaged in commerce.[39] The PNO has accepted that entities with independent legal personality are government agencies where they satisfy some combination of the following criteria:

- they are formed under specific legislation;
- their boards of directors are largely appointed by the government;
- their chief executives are appointed by the government;
- their government must approve their investment plans and budgets;
- they are chartered for the purpose of pursuing a public interest, such as making investments on behalf of the government; and
- the power to dissolve the organization is confirmed to the government.[40]

As a result, when proposing a transaction in the U.S. which would normally be subject to the HSR Act, a SWF may be exempt from the premerger notification requirements if its organization and enabling legislation fit enough of these criteria to satisfy the PNO that it is a government agency.

Although some SWFs do not sufficiently satisfy these criteria, they may still be exempt from the HSR Act's premerger notification requirements on other grounds. For instance, a SWF that is not a corporation would not be considered an entity for HSR purposes. Even for those SWFs that are in corporate form, the determination of whether an organization is a corporation for purposes of the statute is whether it issues ''voting securities'', i.e., ''any securities which at present or upon conversion entitle the owner or holder thereof to vote for the election of directors of the issuer, or of an entity included within the same person as the issuer.''[41] Therefore, if a SWF in corporate form does not issue voting securities as defined above, then it should not be considered a ''corporation'' under the statute and thereby be an ''entity'' subject to the premerger notification requirements (provided, of course, that it does not qualify

[33] *Id.*

[34] Sara Forden, *Obama Bars Chinese-Owned Company from Building Wind-Farm*, Bloomberg News (September 28, 2012).

[35] Order on the China National Aero-Technology Import and Export Corporation Divestiture of MAMCO Manufacturing, Incorporated (February 1, 1990).

[36] Order Regarding the Acquisition of Four U.S. Wind Farm Project Companies by Ralls Corporation (September 28, 2012).

[37] FTC Premerger Notification Office, *What is the Premerger Notification Program? An Overview* (revised March 2009) (available at: *http://www.ftc.gov/bc/hsr/introguides/guide1.pdf*).

[38] 16 C.F.R. § 801.1(a)(2).

[39] Interpretation 11, ABA Premerger Notification Practice Manual (4th ed. 2007).

[40] Informal Staff Opinion 0811007 (November 17, 2008); Informal Staff Opinion 9503021 (March 23, 1995); Informal Staff Opinion 0903003 (March 4, 2009); Informal Staff Opinion 9302006 (February 18, 1993); Informal Staff Opinion 0805002 (May 6, 2008); Informal Staff Opinion 9503021 (March 23, 1995); Informal Staff Opinion 1103006 (March 14, 2011).

[41] 16 C.F.R. § 801.1(f)(1)(i).

as an ''entity'' for other reasons). There is also an exemption for acquisitions by Foreign Governmental Corporations Engaged in Commerce for acquisitions of assets located within that foreign state or of voting securities or non-corporate interests of an entity organized under the laws of that state.

3. Securities Disclosure Requirements

Persons who own equity securities of U.S. registered companies must file certain forms with the Securities Exchange Commission (''SEC'') if their ownership of such companies exceeds certain thresholds.

Section 16(a) of the Securities Exchange Act of 1934 (the ''Exchange Act'') requires persons who, directly or indirectly, are the beneficial owners of more than 10 percent of any class of registered equity security of an issuer (including preferred stock or other securities convertible into equity securities) to file a statement disclosing such ownership. Filing persons are required to file Form 3 within 10 days of the closing of the transaction that would cause them to cross the 10 percent threshold, and to file Form 4 before the end of the second business day following the date of any transaction leading to a change in such ownership.

Section 13(d) of the Exchange Act requires persons who, directly or indirectly, are the beneficial owners of more than five percent of any class of registered equity security of an issuer to file a statement disclosing such ownership. Disclosures must include the identity and management of the reporting person, the source of funds being used to purchase securities, and the reporting person's intentions with respect to the issuer. If such persons hold less than 20 percent of any class of registered equity security of an issuer and do not intend to exercise control over the issuer through such ownership, then they may file Schedule 13G, a short-form statement. Otherwise, they must file Schedule 13D, a more elaborate long-form statement. In either case, filing persons are required to file within 10 days of the closing of the transaction that would cause the investor to cross the five percent ownership threshold and, in the case of Schedule 13D, amend such schedule upon any material change in either ownership (i.e., one percent or more) or the other information disclosed in the filing.

Section 13(f) of the Exchange Act requires ''institutional investment managers'' exercising investment discretion with respect to accounts holding more than $100 million in registered equity securities of issuers (in the aggregate) to file a statement at the end of each fiscal quarter. Section 13(f)(6)(A) provides that, for purposes of Section 13(f), ''institutional investment manager includes any person, other than a natural person, investing in or buying and selling securities for its own account, and any person exercising investment discretion with respect to the account of any other person.'' Required disclosures include the name of each reportable issuer; the title, class, CUSIP number, number of shares or principal amount; the aggregate fair market value of the securities held in each issuer; and whether the investment manager possesses sole or shared authority to exercise the voting rights evidenced by the securities.

In 2008, the SEC confirmed that each of Sections 16(a), 13(d) and 13(f) of the Exchange Act applies to SWFs.[42]

4. Foreign Sovereign Immunities Act

The Foreign Sovereign Immunities Act of 1976 (the ''FSIA'') provides that foreign governments, including their political subdivisions, agencies and instrumentalities, are immune from the jurisdiction of U.S. federal and state courts, subject to certain exceptions.[43] For purposes of the FSIA, an ''agency'' or ''instrumentality'' of a foreign government includes any separate legal person which is an organ of a foreign government or is majority-owned by a foreign government, and which is neither a U.S. citizen nor created under the laws of any third country.[44] Most, if not all, SWFs would fit this description and are therefore subject to the FSIA. However, an important exception to the jurisdictional immunity provided in the FSIA exists with respect to an action ''based upon a commercial activity carried on in the United States by the foreign state; or upon an act performed in the United States in connection with a commercial activity of the foreign state elsewhere; or upon an act outside the territory of the United States in connection with a commercial activity of the foreign state elsewhere and that act causes a direct effect in the United States.''[45]

Given their commercial nature, the typical investment activities of SWFs generally fit within the commercial activity exception of the FSIA. Nonetheless, the statute still provides some procedural advantages and privileges to SWFs even when they are not immune. For instance, pre-judgment attachment of property is excluded unless immunity from such attachment has been specifically waived and there is a showing that the attachment is to secure satisfaction of later judgment, not to obtain jurisdiction.[46] In addition, if a civil action is brought in state court against a SWF, the defendant may remove it to the federal district court in that district, where any trial will be before a judge without a jury.[47] The SWF has a presumption of immunity under the FSIA, which the plaintiff has the burden of rebutting by showing that the action falls into one of the statute's exceptions.[48] If the plaintiff fails to make such a showing, then the SWF will be afforded immunity, unless, of course, it has otherwise waived immunity.[49]

Recent Behavioral Changes

Several SWFs have recently assumed more visible or active positions in respect of their portfolio companies. A notable example of increased activism is Qatar Holding regarding its investment in Xstrata PLC (''Xstrata''). In February 2012, Glencore International PLC (''Glencore'') proposed a merger of equals with Xstrata, in

[42] Congressional Testimony by Ethiopis Tafara, before the U.S. Senate Committee on Banking, Housing, and Urban Affairs (April 2008) (available at: http://sec.gov/news/testimony/2008/ts0342408et.htm).

[43] 28 U.S.C. § 1604.

[44] 28 U.S.C. § 1603(b).

[45] 28 U.S.C. § 1605(a)(2).

[46] 28 U.S.C. § 1610(d).

[47] 28. U.S.C. §§ 1330(a); 1441(d).

[48] *Butler v. Sukhoi Co.*, 579 F.3d 1307, 1312 (11th Cir. 2009).

[49] *Id.*

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which Glencore already held a 34 percent equity stake. Pursuant to that proposal, each Xstrata shareholder would have received 2.8 shares in Glencore in exchange for each of its shares in Xstrata. Xstrata's board of directors approved the offer. During the pendency of the offer, Qatar Holding, an existing shareholder in Xstrata, purchased additional Xstrata shares so that it held approximately 12 percent of the outstanding shares. This made its approval necessary for the transaction to proceed, because the merger required the approval of the holders of 75 percent of the shares not held by Glencore. Dissatisfied with the initial offer, Qatar Holding requested that Glencore improve its offer by increasing the number of Glencore shares to be received by Xstrata shareholders. Eventually, following a meeting between Qatar Holding and Glencore in early September, 2012, the two parties agreed upon a ratio of 3.05 Glencore shares per Xstrata share, and the Xstrata board of directors recommended that shareholders approve the revised offer, which they eventually did.[50] Qatar Holding's role in Glencore's bid for Xstrata has been described as ''something of a watershed moment when an SWF acts like an activist shareholder. . .[h]eretofore, SWFs have typically been cautious passive investors, a judicious strategy in the past considering the potential in both the U.S. and Europe for intensified regulatory interest in how the investment arms of foreign governments buy up domestic properties.''[51]

Some SWFs have become more vocal in respect of the governance of their portfolio companies. As recently reported, Temasek has requested Standard Chartered PLC, in which it holds an 18 percent stake, to appoint more independent directors, after having abstained earlier this year from voting to reelect the board's nonexecutive directors.[52] And Norges Bank Investment Management (''NBIM''), the manager of the Government Pension Fund of Norway (one of the biggest SWFs in the world), has filed several shareholder proposals regarding corporate governance matters, including requesting that the companies in which it has invested separate the roles of Chairman and CEO.[53] During the latest proxy season, NBIM submitted binding shareholder proposals regarding proxy access rights to the Charles Schwab Corporation, Wells Fargo & Company, CME Group, Inc., the Western Union Company, Staples, Inc. and Pioneer Natural Resources Co.[54] Each of these substantially similar proposals called for an amendment to the company's bylaws to permit shareholders who have collectively held at least one percent of the company's stock for at least one year to designate nominees representing up to one-quarter of the company's directors at any election of directors.[55] In addition, the proposals contained links to lengthier supporting statements on NBIM's website, which included criticism of each company's broader corporate governance policies apart from proxy access.[56]

SWFs have also begun to cooperate with each other in respect of certain investments (''club transactions'') and, in at least one instance, more generally – for example, CIC, GIC and KIA contributed an aggregate of $2.8 billion to Barclays in 2008; GIC and Australia's Future Fund collaborated to invest in a private equity firm, Apax Partners; Qatar Holding and CIC are both significant stockholders in Songbird Estates PLC, the owner of almost 70 percent of Canary Wharf in London; and Qatar Holding and GIC are both investors in BAA Ltd., which owns five airports in the United Kingdom. In addition, in June of 2009, Korea Investment Corporation signed cooperation agreements with Malaysia's Khazanah Fund and KIA.

Conclusion

While it is increasingly difficult to generalize about SWFs, in light of their evolving and differing attributes, it seems safe to say that they appear to be permanent and important members of the investing community. It remains to be seen whether the recent and, so far, narrow trend of SWFs towards activism will become more prevalent, but their sheer size, geographic scope and ability to act quickly, as well as their increasing willingness to invest in different asset categories and regions, will likely ensure that they continue to be placed high on the list of desirable financing sources.

[50] *Glencore and Xstrata: Miner irritations*, The Economist (September 15, 2012); Dana Cimilluca and Alex MacDonald, *Xstrata Board Recommends Glencore Deal*, The Wall Street Journal (October 1, 2012); Dana Cimilluca and Alex MacDonald, *Xstrata Shareholders Back Deal Without Retention Packages*, The Wall Street Journal (November 20, 2012).

[51] Richard Levick, *Game-Changer: Qatar Plays Historic Role in Glencore's Bid for Xstrata*, Forbes (September 12, 2012).

[52] P.R. Venkat, *Temasek Answers Standard Chartered*, The Wall Street Journal (October 5, 2012).

[53] F.H. Byrd, *Norges Bank on Proxy Access* (February 24, 2012) (the ''Byrd Interview'') (available at: http://www.laurelhill.com/byrdwatch/byrdwatchi49.aspx).

[54] Press Release, Norges Bank, *NBIM seeks proxy access at six US companies* (December 6, 2011) (available at: http://www.norges-bank.no/en/about/published/press-releases/2011/nbim-seeks-proxy-access).

[55] The Charles Schwab Corp., Proxy Statement (Form 14A) (March 30, 2012); Wells Fargo & Co., Proxy Statement (Form 14A) (March 15, 2012); CME Group Inc., Proxy Statement (Form 14A) (April 25, 2012); Western Union Co., Proxy Statement (Form 14A) (April 10, 2012).

[56] *Id.*