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High Court's Good News For Out-Of-State Parent Companies

By **Gary Mennitt, H. Joseph Escher III and Lily North**

Law360, New York (August 4, 2017, 3:14 PM EDT) -- In the modern world, large-cap and medium-cap businesses often consist of multiple legal entities that function together yet have distinct roles and responsibilities — whether they are bankruptcy-remote special purpose entities that will secure financing, upstream parent entities designed to obtain mezzanine loans, or holding companies that will be the single taxpayer for "look-through" subsidiaries disregarded from a tax perspective.

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For civil litigators on the defense side, consciousness of entity separateness is a must. But for those on the other side of the "v," the common refrain is that affiliated defendants are but one functioning company unified by vicarious liability through single enterprise or alter ego or veil piercing.

Thus, when a plaintiff decides to sue based on the alleged wrongs of an affiliate, a parent or subsidiary company may find itself a party to litigation to which it considers itself a stranger. Even if the vicarious liability allegations are inaccurate, the war that must be waged to prevail on that heavily fact-specific issue may not be worth the fight.

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Well-pleaded allegations designed to disregard the corporate form are likely to make it past a motion to dismiss. Even at the summary judgment stage, sympathetic judges may find plausible some triable question of fact sufficient to deny dismissal. Along the way, savvy plaintiffs' counsel, with sufficiently deep pockets, may use vicarious liability allegations to elicit sensitive financial discovery and "apex" depositions of top executives.

Lily North

For foreign parent defendants, however, the vicarious liability sand trap can be avoided, or at least overcome, early on, through a Rule 12(b)(2) motion to dismiss (or the state law equivalent) for lack of personal jurisdiction. The benefit of this pre-discovery maneuver, when available, can hardly be overstated.

At the motion to dismiss stage, defendants usually are limited to purely legal defenses and obliged to accept as true plaintiff's recitation of the facts, except in the relatively rare cases that the allegations do not meet the federal Rule 8 notice

pleading standard (or fact pleading standard in some state jurisdictions) or can be contradicted by some fact appropriate for judicial notice.

But jurisdictional allegations and Rule 12(b)(2) motions are different. Once jurisdictional allegations are countered by a defensive motion or evidence that jurisdiction is lacking, plaintiff carries the burden to prove, and not just plead, that the court is not overstepping its jurisdictional bounds.

Two U.S. Supreme Court opinions issued this term have only cemented the power of this early maneuver. The Supreme Court issued complimentary opinions on both prongs of the personal jurisdiction analysis: general or "at home" personal jurisdiction and specific or suit-related personal jurisdiction. In both opinion, the court's message is clear: absent being formed or based in a state or directly contributing to the alleged in-state wrong, a defendant is not within a state's jurisdictional reach.

The Supreme Court tackled general jurisdiction in the May 2017 consolidated opinion in BNSF Railway Co. v. Tyrrell, No. 16-405, 137 S. Ct. 1549 (U.S. May 30, 2017). Plaintiffs attempted to sue BNSF Railway in Montana, although plaintiffs did not reside in Montana and were not injured in Montana. Id. at 1553.

General jurisdiction would be proper in Montana, plaintiffs argued, because of BNSF Railway's substantial ties to Montana, including more than 2,000 miles of railroad track and more than 2,000 workers in Montana. Id. at 1559.

Not so, held the Supreme Court, in an opinion written by Justice Ginsburg. Reasoning from the Due Process Clause of the Fourteenth Amendment and the court's landmark opinion in International Shoe Co. v. Washington, 326 U.S. 310 (1945), the court held that general jurisdiction may be exercised over corporations only if "their affiliations with the State are so 'continuous and systematic' as to render them essentially at home in the forum state." Id. at 1552.

"The 'paradigm' forums in which a corporate defendant is 'at home'" are "the corporation's place of incorporation and its principal place of business." Id. (quoting Daimler AG v. Bauman, 134 S. Ct. 746, 760 (2014)). BNSF Railway is not incorporated or based in Montana, and thus, notwithstanding the "magnitude of" its significant operations in the forum, the exercise of general personal jurisdiction would be unconstitutional. BNSF Railway Co. 137 S. Ct. at 1559 (quoting Daimler AG, 134 S. Ct. at 762 n.20).

The Supreme Court next tackled specific or "transactional" jurisdiction in the June 2017 opinion in the multi-state class action case Bristol-Myers Squibb Co. v. Superior Court of Cal., S.F. Cty., No. 16-466, 137 S. Ct. 1773, 1777 (U.S. June 19, 2017).

The Supreme Court rejected non-California resident plaintiffs' attempt to sue Bristol-Myers Squibb in California. The court held that provision of pharmaceuticals to California residents could not create specific jurisdiction over claims of plaintiffs who were not prescribed, did not purchase and did not ingest pharmaceuticals in California. Id. at 1781, 1784.

Starting again from the Due Process Clause of the Fourteenth Amendment and International Shoe Co., Justice Alito, writing for the majority, reiterated that "'the suit' must 'arise out of or relate to the defendant's contacts with the forum." Id. at 1780. Bristol-Myer Squibb had no interactions with the non-California plaintiffs in California, and Bristol-Myers Squibb's interactions with California plaintiffs did not extend jurisdiction to out-of-state plaintiffs.

As in the case of the general jurisdiction, the "primary concern" of due process in a specific personal jurisdiction analysis is "the burden on the defendant." Bristol-Myers Squibb Co., 137 S. Ct. at 1780. As a consequence of American federalism, respecting "the sovereignty of each State implies a limitation on the sovereignty of all its sister States." Id. (quoting World-Wide Volkswagen Corp. v. Woodson, 444 U.S. 286, 293 (1980)).

The mere fact that it could have been more convenient and efficient to litigate the claims of the non-Californians with those of the Californians in the same forum was not enough to make the exercise of jurisdiction over the pharmaceutical company constitutional.

Even though it may be disquieting, federalism requires that constitutional limits be respected and even minimal or no inconvenience on an out-of-state defendant outweighs "a [state's] strong interest in applying its law to the controversy. ..." Bristol-Myers Squibb Co., 137 S. Ct. at 1780–81 (quoting World-Wide Volkswagen, 444 U.S. at 294).

Although the Supreme Court has not recently weighed in on a fact pattern where a subsidiary company does not dispute jurisdiction and a foreign parent does, emerging American jurisprudence should strengthens the argument that a parent is not susceptible to be sued in every U.S. jurisdiction, but only in those jurisdictions where it is "at home" or has taken specific action (or inaction where action was required) leading to a specific lawsuit.

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