CIVIL PROCEDURE: PERSONAL JURISDICTION OVER FOREIGN CORPORATIONS—THE ECONOMIC REALITY APPROACH

THE AUTHORITY of a state to require a foreign corporation to submit to the personal jurisdiction of its courts has been a difficult and frequently litigated problem.[1] Although the issue has remained the same, the context in which it is discussed constantly changes as the states seek to extend their jurisdictional power. A recent New Jersey case, *Hoagland v. Springer*,[2] dealt with this question in an action arising from an explosion in New Jersey of a truck engine sold and installed in Michigan.

The defendant, Cummins Diesel Michigan, Inc., was one of 50 independent distributors of an Indiana manufacturer. Working under distributorship arrangements involving close ties with the manufacturer and cooperation among distributors, defendant frequently exchanged needed parts with its New Jersey counterpart, and the latter was occasionally authorized to service engines sold by the defendant. Nationwide service to customers made possible by this type of cooperation was used to promote defendant's business.

The *Hoagland* case arose when defendant authorized the New Jersey distributor to repair a diesel truck engine previously sold and installed by defendant in Michigan. Subsequently, on the New Jersey Turnpike, the engine exploded and the driver of the truck was injured. Action for damages was instituted by the driver against defendant and others in New Jersey, with service of process being made on Cummins Diesel Michigan, Inc. by registered mail. Upon challenge of its jurisdiction, the court concluded that the economic realities of the arrangement among the manufacturer and the distributors yielded "one, cohesive, economic unit" in the pursuit of business profits and supported assertion of jurisdiction over the Michigan defendant.[3]

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[1] See generally Kurland, *The Supreme Court, the Due Process Clause and the In Personam Jurisdiction of State Courts—From Pennoyer to Denckla: A Review*, 25 U. CHI. L. REV. 569 (1958); *Developments in the Law—State-Court Jurisdiction*, 73 HARV. L. REV. 909, 919-34, 998-1017 (1960); Note, 47 GEO. L.J. 342 (1958).

[2] 75 N.J. Super. 560, 183 A.2d 678 (App. Div.), *aff'd per curiam*, 39 N.J. 32, 186 A.2d 679 (1962).

[3] *Id.* at 569, 183 A.2d at 683.

At common law the situation in the instant case would have precluded jurisdiction, since the requirement of physical power[4] over the defendant coupled with the federal nature[5] of our court system limited jurisdiction to the state of incorporation. However, it was clear from the outset that this jurisdictional concept is not suited to dealing with a corporate entity whose existence is manifested only through the acts of its agents, particularly since these acts are neither limited to nor necessarily focused in the state of its creation. With the tremendous expansion of commerce,[6] the pressure and need for more liberal jurisdictional standards led to the adoption of other theories on which jurisdiction could be based, including, *inter alia,* a presumed right of a state to coerce consent to suit as a price for doing business or an inferred presence of a corporation from the extent and manner of its activities.[7]

These rigid, fictional determinants soon proved equally unsatisfactory and the necessity of their existence was discarded by the Supreme Court in *International Shoe Co. v. Washington.*[8] In their place, the flexible standard of fair play and substantial justice required by the due process clause of the fourteenth amendment was put forth as the only limitation.[9] In applying the *International Shoe* doctrine to specific fact situations, the Supreme Court has found that even a single contact by mail may be sufficient to support jurisdiction.[10] Furthermore, the fact that the cause of action does not arise out of defendant's activities within the state is not fatal.[11] However, a territorial restriction yet remains in that defendant must initiate some act by which he purposefully avails himself of the benefits and privileges of the forum state.[12] In the *Hoagland* case this territorial interest requirement was easily fulfilled by the interstate commercial dealings among distributors.

[4] See HENDERSON, THE POSITION OF FOREIGN CORPORATIONS IN AMERICAN CONSTITUTIONAL LAW 77-80 (1918).

[5] See Sobeloff, *Jurisdiction of State Courts Over Non-Residents in Our Federal System,* 43 CORNELL L.Q. 196, 197-200 (1957); Stimson, *Omnibus Statutes Designed to Secure Jurisdiction Over Out-of-State Defendants,* 48 A.B.A.J. 725 (1962).

[6] The effect of this expansion is discussed in Hanson v. Denckla, 357 U.S. 235, 250-51 (1958), and McGee v. International Life Ins. Co., 355 U.S. 220, 222-23 (1957).

[7] See Kurland, *supra* note 1, at 577-86; *Developments in the Law—State-Court Jurisdiction,* 73 HARV. L. REV. 909, 919-23 (1960); Note, 47 GEO. L.J. 342, 347-48 (1958).

[8] 326 U.S. 310 (1945).

[9] *Id.* at 316-19.

[10] McGee v. International Life Ins. Co., 355 U.S. 220 (1957).

[11] Perkins v. Benguet Consol. Mining Co., 342 U.S. 437 (1952).

[12] See Hanson v. Denckla, 357 U.S. 235 (1958).

Since New Jersey statutory limitations add no further restrictions, the *Hoagland* court had to consider only the limitations imposed on its jurisdiction by the due process clause of the fourteenth amendment.[13] However, in factual situations similar to that found in the instant case, many courts have felt constrained to look for some agency relationship[14] or to examine the degree of control exercised over the domestic entity.[15] Such tests have value in that, where agency or control is found, this is sufficient evidence of satisfactory contacts to insure fairness. However, courts utilizing this analysis will fail to assert the full extent of jurisdiction allowed by the Constitution.[16]

In the *Hoagland* case, although the court found sufficient "uncontroverted facts" to warrant recognition of the New Jersey distributor as a special agent of the defendant,[17] it chose to avoid involvement with such restrictive factors and based its decision on the broader ground of economic reality. Accordingly, the mechanics, purpose, and effect of the economic relationship between the distributors and the manufacturer were examined. The court found that defendant's scheme for success depended partially upon dealings with the New Jersey distribtuor which resulted in an economic benefit to the defendant.[18] Being unwilling to allow defendant "the fruits of its New Jersey activities without the attendant liabilities,"[19] the court granted jurisdiction.

Previously, New Jersey courts have interpreted due process to re-

[13] N.J. REVISED RULES 4:4-4(d) provides that service of process can be made on a foreign corporation by registered mail "subject to due process of law." This, of course, parallels the constitutional requirement and has been so interpreted by the New Jersey courts. See Dowd v. Boro Drugs, Inc., 70 N.J. Super., 488, 495-98, 176 A.2d 13, 17-19 (App. Div. 1961).

[14] See, *e.g.*, Supreme Wine Co. v. Distributors of New England, Inc., 198 F. Supp. 318 (D. Mass. 1961) (corporation held agent of defendant where it sold exclusively defendant's product); Shoultz v. Revolvator Co., 186 F. Supp. 61 (E.D. Pa. 1959) (sales representative did not have power to bind its principal); H. F. Campbell Constr. Co. v. Palombit, 347 Mich. 340, 79 N.W.2d 915 (1956) (dealer who received goods on consignment held agent).

[15] See, *e.g.*, Kahn v. Maico Co., 216 F.2d 233 (4th Cir. 1954) (selling price, advertising, and other policies controlled); Republic Supply Corp. v. Lewyt Corp., 160 F. Supp. 949 (E.D. Mich. 1958) (substantial control through distributorship contract); Jarrard Motors, Inc. v. Jackson Auto & Supply Co., 237 Miss. 660, 115 So. 2d 309 (1959) (distributor possessed absolute control over dealer's method and manner of doing business).

[16] See note 32 *infra*.

[17] 75 N.J. Super. at 569, 183 A.2d at 683.

[18] *Ibid.*

[19] *Id.* at 570, 183 A.2d at 684.

quire that the cause of action must arise out of defendant's activities within the forum state.[20] Although this connection may be implicit in the eventual decision,[21] the court did not attempt to relate the cause of action to defendant's contacts prior to examining them in the light of fair play and substantial justice.[22] It could be inferred, therefore, that the court did not consider fair play and substantial justice to depend upon such an intermediate analysis.

The logical extension of the economic reality approach adopted by this court would seem to be: Whenever there is exploitation of the forum state for profit by a non-resident, it is not unreasonable to allow jurisdiction, subject always to other factors bearing on fairness. However, it does not necessarily follow that where there is no exploitation there will be no jurisdiction, since other contacts may appear which will establish the requisite fairness.[23]

This approach would also seem applicable to those situations in which a domestic corporation is a subsidiary of a foreign corporation and jurisdiction of the parent is sought on the basis of its activities in the forum state through its subsidiary. At one point in the *Hoagland* opinion the court said that it was not important that

[20] See, *e.g.*, Malavasi v. Villavecchia, 62 N.J. Super. 510, 163 A.2d 214 (L. 1960); Note, 47 GEO. L.J. 342, 353-55 (1958). See also Reese & Galston, *Doing an Act or Causing Consequences as Bases of Judicial Jurisdiction*, 44 IOWA L. REV. 249, 264 (1959) (suggests broadening of the requirement to include consequences occurring within the state). *But see* 108 U. PA. L. REV. 131 (1959), for a critical appraisal of this approach as applied by a federal court to a suit brought in California.

[21] Ample support can be found, however, for defendant's contention that the cause of action, if any, arose out of defendant's acts in Michigan. See Johns v. Bay State Abrasive Prods. Co., 89 F. Supp. 654 (D. Md. 1950); Rufo v. Bastian-Blessing Co., 405 Pa. 12, 173 A.2d 123 (1961). A few states might look to the injury as the consummation of a tort within the state and rest jurisdiction upon that basis. See Gray v. American Radiator & Standard Sanitary Corp., 22 Ill. 2d 432, 176 N.E.2d 761 (1961); Atkins v. Jones & Laughlin Steel Corp., 258 Minn. 571, 104 N.W.2d 888 (1960).

[22] Nor would the pronouncements of the Supreme Court seem to require such a relationship. In International Shoe Co. v. Washington, 326 U.S. 310 (1945), it was stated that: "[T]here have been instances in which the continuous corporate operations within a state were thought so substantial and of such a nature as to justify suit against it on causes of action arising from dealings entirely distinct from those activities. . . . It is evident that the criteria by which we mark the boundary line between those activities which justify the subjection of a corporation to suit, and those which do not, cannot be simply mechanical or quantitative. . . . Whether due process is satisfied must depend rather upon the quality and nature of the activity in relation to the fair and orderly administration of the laws which it was the purpose of the due process clause to insure." *Id.* at 318-19. *Accord*, Perkins v. Benguet Consol. Mining Co., 342 U.S. 437 (1952).

[23] See Hess v. Pawloski, 274 U.S. 352 (1927) (non-resident motorists statute); Nelson v. Miller, 11 Ill. 2d 378, 143 N.E.2d 673 (1957) (commission of a tortious act within the state).

the Indiana manufacturer chose to sell its goods through independent distributors.[24] Logically, therefore, it should be equally unimportant that a parent corporation chooses to sell through its subsidiary,[25] since the "economic well-being"[26] of each unit of the empire still directly affects the success of the other units.

Presently, however, courts faced with the jurisdictional question in such parent-subsidiary situations look solely to the extent to which the formalities of the separate entity concept have been preserved.[27] If the corporate formalities have been maintained, the parent's position is, analytically, the same as that of any other independent contractor dealing with the subsidiary, and it should be subject to jurisdiction on the same basis.[28] Applying an economic reality approach would lead to allowing jurisdiction whenever the operational purposes of the parent and subsidiary were intertwined. For example, where the subsidiary was formed for the purpose of selling the parent's products, its operational purposes would support jurisdiction. The emphasis thus would be taken away from the form of the business relationship and placed on the purpose and result. This should more satisfactorily insure the "fair play and substantial justice"[29] sought to be preserved by the due process requirement.

Exploitation of a state by a foreign corporation should prove to be a constitutionally acceptable basis for the further breakdown of territorial jurisdictional limitations and, as such, is of value.[30] How-

[24] 75 N.J. Super. at 569, 183 A.2d at 683.

[25] See Foster, *Personal Jurisdiction Based on Local Causes of Action*, 1956 WIS. L. REV. 522, 563. *But see* Dowd v. Boro Drugs, Inc., 70 N.J. Super. 488, 503-04, 176 A.2d 13, 22 (App. Div. 1961) (dictum).

[26] 75 N.J. Super. at 569, 183 A.2d at 683.

[27] See leading case of Cannon Mfg. Co. v. Cudahy Packing Co., 267 U.S. 333 (1925), where the court found the subsidiary to be completely dominated by the parent but denied jurisdiction because they were distinct corporate entities. *Accord*, Harris v. Deere & Co., 223 F.2d 161 (4th Cir. 1955); Fergus Motors, Inc. v. Standard-Triumph Motor Co., 130 F. Supp. 780 (S.D.N.Y. 1955); Dowd v. Boro Drugs, Inc., 70 N.J. Super. 488, 503-04, 176 A.2d 13, 22 (App. Div. 1961) (dictum). See Note, 56 COLUM. L. REV. 394, 409-10 (1956); Note, 44 IOWA L. REV. 345, 358-59 (1959).

[28] See Empire Steel Corp. v. Superior Court, 56 Cal. 2d 823, 829-30, 834-35, 366 P.2d 502, 505-06, 509, 17 Cal. Rptr. 150, 153-54, 157 (1961), 9 U.C.L.A.L. REV. 249 (1962); Note, 104 U. PA. L. REV. 381, 403-06 (1955).

[29] International Shoe Co. v. Washington, 326 U.S. 310, 316 (1945).

[30] The constitutionality of such an extension would seem to follow as another product of the increasing trend of commerce to become national in scope. This has been the moving force behind changing previous concepts of jurisdictional limitations. *Compare* International Shoe Co. v. Washington, 326 U.S. 310, 319 (1945), where it was stated that in most instances it is not unreasonable to require a foreign corporation

ever, it is doubtful that even the *Hoagland* court will accept the suggested implications and extensions of its rationale within the immediate future.[31] But the step is a short one, and the movement of other states toward the same ultimate end should provide impetus for such recognition.[32]

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conducting activities within a state and enjoying the benefits and protections of the laws of that state to respond to a suit resulting from those activities, *with* the implications of the *Hoagland* decision, which seem equally reasonable. A corporation which obtains a profit from the forum state through activities conducted in the normal course of its business has *per se* received the benefits and protection of the laws of that state and should accordingly be subject to the jurisdiction of state tribunals.

[31] See the recent decision by the same court in Dowd v. Boro Drugs, Inc., 70 N.J. Super. 488, 176 A.2d 13 (App. Div. 1961), where the court dismissed a previous decision as not being made on a business relationship rationale. The court also, in dictum, recognized the continuing vitality of the doctrine enunciated in Cannon Mfg. Co. v. Cudahy Packing Co., 267 U.S. 333 (1925), that, where the parent and its subsidiary are separate corporate entities, jurisdiction must be denied.

[32] Several states have specifically provided by statute that sending products into the state for use, sale, etc., will subject the parties concerned to the jurisdiction of the state's courts. See CONN. GEN. STAT. REV. § 33-411 (c) (3) (Supp. 1959); FLA. STAT. § 47.16 (1961); N.C. GEN. STAT. § 55-145 (a) (3) (1960). These statutes should provide a result similar to that of the economic reality approach of the New Jersey Court in the instant case and should arrive at that position more quickly and with more certainty. However, even with these specific statutes, the extent of jurisdiction taken will still depend upon the willingness of courts to exercise the full power granted. See Berkman v. Ann Lewis Shops, Inc., 246 F.2d 44 (2d Cir. 1957) (FLA. STAT. § 47.16 held not to overrule the separate entity doctrine of Cannon Mfg. Co. v. Cudahy Packing Co., *supra* note 31); Jenkins v. Fawcett Publications, Inc., 204 F. Supp. 361 (N.D. Fla. 1962) (FLA. STAT. § 47.16 construed narrowly); Putnam v. Triangle Publications, Inc., 245 N.C. 432, 96 S.E.2d 445 (1957) (N.C. GEN. STAT. § 55-38.1 (a) (3) [now § 55-145 (a) (3)] held unconstitutional as applied to the facts of the case).

Illinois and Minnesota have achieved a similar result through judicial interpretation of statutes allowing jurisdiction where a tortious act is committed within the state. See Gray v. American Radiator & Standard Sanitary Corp., 22 Ill. 2d 432, 176 N.E.2d 761 (1961); Atkins v. Jones & Laughlin Steel Corp., 258 Minn. 571, 104 N.W.2d 888 (1960).